

In the opinion of Hawkins, Delafield & Wood, Bond Counsel, under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein: (i) interest on the Senior Series 2003A Bonds is excluded from gross income for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"); and (ii) interest on the Senior Series 2003A Bonds, however, is treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code. In addition, in the opinion of Bond Counsel, under existing statutes, the Senior Series 2003A Bonds and the income thereon and the transfer thereof, including any profit made on the sale thereof, shall at all times be exempt from taxation or assessment of any type by the Commonwealth, its agencies and departments and by all political subdivisions within the Commonwealth. See "TAX MATTERS" herein for a description of certain other provisions of the Code that may affect the tax treatment of interest on the Senior Series 2003A Bonds for certain Bondholders.

**NEW ISSUE - Book-Entry Only**



**\$80,650,000**

**Kentucky Higher Education Student Loan Corporation**

**\$63,700,000 Student Loan Revenue Bonds, Senior Series 2003A-1**

**\$16,950,000 Student Loan Revenue Bonds, Senior Series 2003A-2**

**(Auction Rate Certificates-ARCs®)**

**Dated:** Date of Delivery

**Price:** 100%

**Due:** May 1, 2033

The Senior Series 2003A-1 Bonds (the "Senior Series 2003A-1 Bonds") and the Senior Series 2003A-2 Bonds (the "Senior Series 2003A-2 Bonds" and, collectively with the Senior Series 2003A-1 Bonds, the "Senior Series 2003A Bonds") are issuable in fully-registered form and when issued shall be registered in the name of Cede & Co. as nominee for The Depository Trust Company, New York, New York ("DTC"), which shall act as Securities Depository for the Senior Series 2003A Bonds. Purchasers of the Senior Series 2003A Bonds will not receive certificates representing their beneficial ownership interests in the Senior Series 2003A Bonds. Purchases and sales by the Beneficial Owners (as defined herein) of the Senior Series 2003A Bonds shall be made in book-entry form in the principal amount of \$50,000 or any integral multiple thereof. See "BOOK-ENTRY SYSTEM" herein.

Payments of principal, redemption price, and interest with respect to the Senior Series 2003A Bonds are to be made directly to DTC by Bank One, NA (the "Trustee" and "Paying Agent") or its successor Trustee, so long as DTC or Cede & Co. is the registered owner of the Senior Series 2003A Bonds. Disbursements of such payments to DTC Participants (as defined herein) are the responsibility of DTC and the disbursements of such payments to the Beneficial Owners are the responsibility of DTC Participants as more fully described herein.

The Senior Series 2003A Bonds are being issued by the Kentucky Higher Education Student Loan Corporation (the "Corporation"), an independent *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky, pursuant to the provisions of the 1997 General Bond Resolution adopted by the Corporation on May 9, 1997 (as heretofore amended, and as further amended by the Supplemental Resolution adopted by the Corporation on May 6, 2003, the "General Bond Resolution") and pursuant to the Series 2003A-1 and Series 2003A-2 Bond Resolution (the "Series 2003A Bond Resolution") adopted by the Corporation on May 6, 2003.

The Senior Series 2003A Bonds are being issued as Auction Rate Certificates-ARCs® ("ARCs") in denominations of \$50,000 or any integral multiple thereof. Interest on the Senior Series 2003A Bonds, prior to a change in the Interest Payment Dates as described herein, shall be payable on November 1, 2003 and semiannually on each May 1 and November 1 thereafter until maturity or earlier redemption.

The Senior Series 2003A-1 Bonds are being issued to provide funding for the origination or purchase of Student Loans (as defined herein). The Senior Series 2003A-2 Bonds are being issued to provide funding for: (i) the origination or purchase of Student Loans through the payment of advances under a Line of Credit Agreement Note dated as of November 1, 2000 between the Corporation and Bank of America, N.A., which advances were used to refund \$1,200,000 principal amount of the Corporation's Student Loan Revenue Bonds, Series 1991B, and to refund \$295,000 principal amount of the Corporation's Student Loan Revenue Bonds, Series 1991D, and (ii) refunding or optional redemption of certain of the Corporation's outstanding Bonds. See "USE OF PROCEEDS" herein.

The Senior Series 2003A Bonds will be equivalent in right of payment under the General Bond Resolution with the Senior Series 2002A Bonds, the Senior Series 2001A Bonds, the Senior Series 2000A Bonds, the Senior Series 2000B Bonds, the Senior Series 1999A Bonds, the Senior Series 1999B Bonds, the Senior Series 1998A Bonds, the Senior Series 1998B Bonds and the Senior Series 1997-A Bonds, and with all other Senior Obligations that may be issued thereunder in the future, and are senior in right of payment under the General Bond Resolution to the Subordinate Series 2001B Bonds and the Subordinate Series 1997-B Bonds, and to all Senior Subordinate Obligations and Subordinate Obligations that may be issued thereunder in the future. The Senior Series 2003A Bonds are subject to redemption prior to maturity and mandatory tender for purchase as described herein.

**THE SENIOR SERIES 2003A BONDS ARE SPECIAL AND LIMITED OBLIGATIONS OF THE CORPORATION, SECURED BY AND PAYABLE FROM SPECIFIC REVENUES, FUNDS, AND ASSETS PLEDGED THEREFOR AS HEREIN DESCRIBED. THE SENIOR SERIES 2003A BONDS DO NOT CONSTITUTE A DEBT OF THE COMMONWEALTH OR ANY POLITICAL SUBDIVISION THEREOF. THE PAYMENT OF THE PRINCIPAL OF AND INTEREST ON THE SENIOR SERIES 2003A BONDS IS NOT SECURED BY A PLEDGE OF THE FAITH AND CREDIT OR THE TAXING POWER OF THE COMMONWEALTH OR ANY POLITICAL SUBDIVISION THEREOF. KENTUCKY'S NAME IS ON THE SENIOR SERIES 2003A BONDS FOR THE BENEFIT AND CONVENIENCE OF OTHER ENTITIES IN THE COMMONWEALTH. HOWEVER, THE ONLY SECURITY THAT IS PLEDGED FOR THE SENIOR SERIES 2003A BONDS IS THE INDEPENDENT REVENUES AND ASSETS FROM THE PROJECT. THE GENERAL ASSEMBLY DOES NOT INTEND TO APPROPRIATE ANY COMMONWEALTH FUNDS TO FULFILL THE FINANCIAL OBLIGATIONS REPRESENTED BY THE SENIOR SERIES 2003A BONDS. THE CORPORATION HAS NO TAXING POWER.**

The Senior Series 2003A Bonds are offered when, as and if received by the Underwriter, subject to prior sale, to withdrawal or modification of the offer without notice and to the approval of legality by Hawkins, Delafield & Wood, New York, New York, Bond Counsel.

Certain legal matters in connection with the Senior Series 2003A Bonds will be passed upon for the Underwriter by its counsel, Squire, Sanders & Dempsey L.L.P. The Senior Series 2003A Bonds are expected to be available for delivery in New York, New York on or about May 20, 2003.

**UBS PaineWebber Inc.**

Dated: May 14, 2003

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The information set forth herein has been obtained from the Corporation, the Kentucky Higher Education Assistance Authority ("KHEAA") and other sources that are believed to be reliable, but is not guaranteed as to accuracy or completeness, and is not to be construed as a representation, by the Underwriter. The information and expressions of opinion contained herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Corporation or KHEAA or that the information or opinions or estimates contained herein are correct as of any date subsequent to the date hereof.

No dealer, broker, salesman or other person has been authorized by the Corporation, KHEAA or the Underwriter to give any information or to make any representations with respect to the Senior Series 2003A Bonds, other than those contained herein, and if given or made, such other information or representations must not be relied upon as having been authorized by any of the foregoing. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Senior Series 2003A Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale.

**Except for any information provided by the Trustee concerning the Trustee, the Trustee has no responsibility for any information in this Official Statement. Further, the Trustee shall have no responsibility for compliance with any state or federal securities laws in connection with the Senior Series 2003A Bonds, except to the extent that the Trustee has agreed to forward continuing disclosure materials received from and prepared by the Corporation to the appropriate Repository.**

**IN MAKING AN INVESTMENT DECISION, INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE CORPORATION AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS AND RISKS INVOLVED. THE SENIOR SERIES 2003A BONDS HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS OFFICIAL STATEMENT.**

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## OFFICIAL STATEMENT

**KENTUCKY HIGHER EDUCATION STUDENT LOAN CORPORATION**  
**\$63,700,000 Student Loan Revenue Bonds, Senior Series 2003A-1**  
**\$16,950,000 Student Loan Revenue Bonds, Senior Series 2003A-2**  
**(Auction Rate Certificates-ARCs®)**

### INTRODUCTION

This Official Statement sets forth certain information concerning the Kentucky Higher Education Student Loan Corporation (the “Corporation”), an independent *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky (the “Commonwealth”), and its issue of \$80,650,000 in aggregate principal amount of Student Loan Revenue Bonds, consisting of \$63,700,000 Student Loan Revenue Bonds, Senior Series 2003A-1 (the “Senior Series 2003A-1 Bonds”) and \$16,950,000 Student Loan Revenue Bonds, Senior Series 2003A-2 (the “Senior Series 2003A-2 Bonds” and, collectively with the Senior Series 2003A-1 Bonds, the “Senior Series 2003A Bonds”). The Senior Series 2003A Bonds are being issued pursuant to the provisions of Sections 164A.010 to 164A.240, Kentucky Revised Statutes, as amended (the “Act”), the 1997 General Bond Resolution adopted by the Corporation on May 9, 1997, (as heretofore amended, and as further amended by the Supplemental Resolution adopted by the Corporation on May 6, 2003, the “General Bond Resolution”), and the Series 2003A-1 and Series 2003A-2 Bond Resolution adopted by the Corporation on May 6, 2003 (the “Series 2003A Bond Resolution” and, collectively with the General Bond Resolution, the “Resolutions”). Capitalized terms used and not otherwise defined herein shall have the meanings given them in Appendix B, “DEFINITIONS OF CERTAIN TERMS” and Appendix F, “AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS”.

The Senior Series 2003A Bonds constitute Additional Obligations pursuant to the General Bond Resolution. The Corporation has heretofore issued several Series of its Student Loan Revenue Bonds thereunder, of which \$700,150,000 Senior Obligations and \$74,850,000 Subordinate Obligations remain Outstanding. The General Bond Resolution permits the issuance of additional bonds (the “Additional Bonds”) or other Obligations through the adoption of additional Series Resolutions. The priority of claim as to payment of such Additional Bonds or other Obligations under the Resolutions may be equal to or inferior to the Senior Series 2003A Bonds. The General Bond Resolution also permits the Corporation to enter into Obligation Facilities or Swap Facilities the payment of which by the Corporation shall have the same priority of claim as to payment under the General Bond Resolution as does the Series of Bonds or other Obligations to which such Obligation or Swap Facilities relate.

The Senior Series 2003A Bonds are equivalent in right of payment under the General Bond Resolution with the Senior Series 2002A Bonds, the Senior Series 2001A Bonds, the Senior Series 2000A Bonds, the Senior Series 2000B Bonds, the Senior Series 1999A Bonds, the Senior Series 1999B Bonds, the Senior Series 1998A Bonds, the Senior Series 1998B Bonds and the Senior Series 1997-A Bonds (collectively, the “Prior Senior Bonds”), and with all other Senior Obligations that may be issued thereunder in the future, and are senior in right of payment under the General Bond Resolution to the Subordinate Series 2001B Bonds and the Subordinate Series 1997-B Bonds (the “Prior Subordinate Bonds”), and to all other Senior Subordinate Obligations and Subordinate Obligations that may be issued thereunder in the future. The Series Resolutions for the Prior Senior Bonds and the Prior Subordinate Bonds provide that the Prior Senior Bonds and the Prior Subordinate Bonds originally issued to bear interest at an Auction Rate may be converted to bear interest at a Variable Rate, as more fully described in therein. Contemporaneously herewith, the Corporation is issuing \$40,600,000 in aggregate principal amount of its Insured Student Loan Revenue Bonds pursuant to a General Bond Resolution adopted by the Corporation on June 10, 1983 (the “1983 Resolution”), which are secured as provided in the 1983 Resolution and are not secured by the General Bond Resolution, or by any interest in the funds or other assets pledged under the General Bond Resolution to the payment of the Bonds.

Subject to the provisions of the General Bond Resolution, a Trust Estate including the following assets is pledged to the payment of the principal of, redemption price, if any, and interest on the Senior Series 2003A Bonds, any Additional Bonds and any other Obligations: (i) all moneys, including Bond proceeds, held in any of the funds

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and accounts (other than the Rebate Account) established and held under the Resolutions or received by the Trustee for deposit in such funds and accounts (other than the Rebate Account); (ii) all Loans, the Corporation's right, title and interest in which is funded through the application of assets described in (i) above, along with all documentation thereof and all rights of the Corporation with respect thereto except as expressly provided in the Resolutions; (iii) all guarantee or insurance payments with respect to Loans and interest thereon described in (ii) above; (iv) all other Revenues; and (v) all direct or indirect proceeds of any of the assets described in (i) through (iv) above.

The Senior Series 2003A Bonds are subject to redemption as more fully described herein under the caption "DESCRIPTION OF THE SENIOR SERIES 2003A BONDS—Redemption Provisions". Further, the Series 2003A Bond Resolution provides that the Senior Series 2003A Bonds originally issued as ARCs may be converted to bear interest at a Variable Rate or a Fixed Rate, as more fully described in the Series 2003A Bond Resolution. This Official Statement, in general, describes the Senior Series 2003A Bonds only while they are outstanding as ARCs. See "AUCTION RATE CERTIFICATES—Fixed Rate Conversion of ARCs", "—Variable Rate Conversion of ARCs" and "—Mandatory Tender Upon Conversion; Certain Notices". The Trustee is the initial Paying Agent and Registrar for the Senior Series 2003A Bonds. Descriptions of the Corporation, the Guaranty Agencies (as herein defined), the Senior Series 2003A Bonds, the Corporation's education finance and servicing activities, the Resolutions and related documents are included in this Official Statement. The descriptions of such documents included in this Official Statement do not purport to be comprehensive or definitive and are qualified in their entirety by reference to such documents, which documents are on file with the Trustee.

## USE OF PROCEEDS

The Senior Series 2003A-1 Bonds are being issued to provide funding for the origination or purchase by the Corporation of Student Loans in accordance with the Resolutions and the Act. The Corporation currently expects to apply all Senior Series 2003A-1 Bond proceeds initially available, along with all funds made available therefore as a result of the initial application of Senior Series 2003A-2 proceeds, to finance Student Loans by July 1, 2004 to the origination or purchase of Student Loans that are originated pursuant to the Federal Family Education Loan Program ("FFELP Loans") and are guaranteed by the Kentucky Higher Education Assistance Authority ("KHEAA"). See "DESCRIPTION OF THE SENIOR SERIES 2003A BONDS – Redemption Provisions – *Mandatory Redemption of Senior Series 2003A Bonds from Unexpended Bond Proceeds.*" See "THE CORPORATION—The Corporation's Education Finance and Servicing Activities", "THE GUARANTEE AGENCIES" and Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM". Such Student Loans may include Student Loans that currently secure other Corporation obligations. See "THE CORPORATION—The Corporation's Education Finance and Servicing Activities—*FFELP Loan Financing*".

The Senior Series 2003A-2 Bonds are being issued to provide funding for: (i) the origination or purchase of Student Loans through the payment of advances under a Line of Credit Agreement Note dated as of November 1, 2000 between the Corporation and Bank of America, N.A., which advances were used to refund \$1,200,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1991 Series B, and to refund \$295,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1991 Series D; (ii) refunding on June 1, 2003 the following Bonds, all payable on June 1, 2003: \$400,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1991 Series B; \$375,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1991 Series D; \$750,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1995 Series B; \$3,000,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1995 Series C; \$2,500,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1996 Series B; \$1,000,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1997 Series B; \$1,000,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1997 Series D; and (iii) optional redemption on June 1, 2003 of \$6,430,000 principal amount of the Corporation's Insured Student Loan Revenue Bonds, 1991 Series D. All of the Insured Student Loan Revenue Bonds described in this paragraph were issued under the 1983 Resolution.

The Corporation reserves the right to apply amounts held under the Resolutions to finance FFELP Loans that are guaranteed by Guaranty Agencies other than KHEAA and to finance Student Loans that are not FFELP

Loans, subject to the provisions of the Resolutions. See “THE CORPORATION—The Corporation’s Education Finance and Servicing Activities”. The Corporation expects to apply a portion of the Senior Series 2003A Bond proceeds to pay costs of issuance in connection with the Senior Series 2003A Bonds. The Corporation may transfer funds in the Revenue Account to the Loan Account as permitted by the Resolutions to be used to acquire or originate additional Student Loans until July 1, 2006, unless such date is extended by the Corporation by delivery to the Trustee of a Certificate accompanied by a Rating Affirmation.

## **SOURCES AND USES OF FUNDS**

### Sources

Bond Proceeds	\$80,650,000
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### Uses

Deposit in Loan Account	\$63,291,240
Deposit in 2003 Refunding Escrow Account	\$16,950,000
Estimated Cost of Issuance	<u>\$408,760</u>
 Total Uses	 \$80,650,000

### **Initial Collateralization**

Upon issuance of the Senior Series 2003A Bonds, it is anticipated that the value of the Assets pledged under the General Bond Resolution will be equal to approximately 111.4% of the aggregate principal amount of the then Outstanding Senior Bonds and equal to approximately 101.6% of the aggregate principal amount of all Bonds then Outstanding. The General Bond Resolution does not require that these levels of collateralization be established or maintained.

## **SECURITY AND SOURCES OF PAYMENT FOR THE SENIOR SERIES 2003A BONDS**

### **Limited Liability**

The Senior Series 2003A Bonds are special and limited obligations of the Corporation, secured by and payable from specific revenues, funds, and assets pledged therefore as herein described. The Senior Series 2003A Bonds do not constitute a debt of the Commonwealth or any political subdivision thereof. The payment of the principal of and interest on the Senior Series 2003A Bonds is not secured by a pledge of the faith and credit or the taxing power of the Commonwealth or any political subdivision thereof. Kentucky’s name is on the Senior Series 2003A Bonds for the benefit and convenience of other entities in the Commonwealth. However, the only security that is pledged for the Senior Series 2003A Bonds is the independent revenues and assets from the project. The General Assembly does not intend to appropriate any Commonwealth funds to fulfill the financial obligations represented by the Senior Series 2003A Bonds. The Corporation has no taxing power.

### **The Pledge of the General Bond Resolution**

The Act provides that any pledge made by the Corporation shall be valid and binding from the time made and further provides that the income, revenue or other property so pledged and thereafter received by the Corporation shall immediately be subject to the lien of such pledge without any physical delivery or further act, and that the lien of any such pledge shall be valid and binding as against all parties having claims of any kind in tort, contract or otherwise against the Corporation irrespective of whether such parties have notice thereof.

The General Bond Resolution establishes a pledge of the Trust Estate for the benefit of Owners of all Obligations on a basis of parity and, subject to the provisions of the General Bond Resolution, permitting the application thereof for the purposes of and on the terms and conditions set forth in the General Bond Resolution and

provides that such pledge constitutes a perfected first lien thereon. The Trust Estate includes the following: (i) all moneys, including Bond proceeds, held in any of the funds and accounts (other than the Rebate Account) established and held under the Resolutions or received by the Trustee for deposit in such funds and accounts (other than the Rebate Account); (ii) all Loans, the Corporation's right, title and interest in which is funded through the application of assets described in (i) above, along with all documentation thereof and all rights of the Corporation with respect thereto except as expressly provided in the Resolutions; (iii) all guarantee or insurance payments with respect to Loans and interest thereon described in (ii) above; (iv) all other Revenues; and (v) all direct or indirect proceeds of any of the assets described in (i) through (iv) above.

### **Principal, Interest, Interest Subsidy and Special Allowance Payments on FFELP Loans**

Payments of the principal of and interest on the Loans, along with Interest Subsidy Payments and Special Allowance Payments, if any, with respect to FFELP Loans, are expected to be received by the Corporation in amounts sufficient, together with other revenues and amounts held under the Resolutions, to pay the principal of and interest on the Senior Series 2003A Bonds when due. The Corporation is entitled to receive Interest Subsidy Payments from the Secretary of the United States Department of Education ("Secretary") with respect to each Federal Subsidized Stafford Loan for the entire amount of interest due on such loan during the period the student is in school, during grace periods, and during periods of deferment. During all other periods, interest on Federal Subsidized Stafford Loans is collected from the borrower. See Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Interest Subsidy Payments on Subsidized Stafford Loans". The Corporation is also entitled to receive Special Allowance Payments with respect to FFELP Loans, which the Secretary of Education is required by the Higher Education Act to pay on a quarterly basis. See Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Special Allowance Payments". On Federal PLUS/SLS, Federal Unsubsidized Stafford Loans, and Federal Consolidation Loans, the Corporation collects interest payments from the borrower from the date of loan disbursement. Repayment of Federal Consolidation Loans commences within 60 days of the discharge of the lenders of the consolidated loans. For additional information on the FFELP Loans, see "THE CORPORATION" and "GUARANTY AGENCIES" and Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM".

### **Debt Service Reserve Account**

The Senior Series 2003A Bonds are secured by a Debt Service Reserve Account that is created by the General Bond Resolution and pledged to the security of all Obligations issued under the Resolutions. The Debt Service Reserve Account shall at all times be maintained at a level at least equal to the aggregate requirement therefor established under the Resolutions. Upon issuance of the Senior Series 2003A Bonds, such aggregate requirement will be approximately equal to 1.46% of the aggregate principal amount of Bonds Outstanding, subject to a \$500,000 overall Debt Service Reserve Account minimum aggregate requirement. There is no assurance that the Reserve Account Requirement will be increased or maintained at such level and funded upon the issuance of any Additional Bonds or other Obligations. Upon the issuance of any Additional Bonds or other Obligations, amounts in the Debt Service Reserve Account shall also secure payment of such Additional Bonds or other Obligations in accordance with the priority of payment established under the Resolutions. See Appendix C, "SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS—Establishment of Accounts".

Prior to using any moneys in the Debt Service Reserve Account to make payments with respect to any Obligations, the Trustee is required to use amounts credited as cash to the Loan Account, without liquidating Loans credited thereto, and to deposit such amounts in the Revenue Account for the purpose of making such payments on the Obligations. Under the General Bond Resolution, the Trustee is required, on each Interest Payment Date, to transfer from the Revenue Account to the Debt Service Reserve Account, the amount, if any, necessary to cause the Debt Service Reserve Account to be funded at the Reserve Account Requirement, subsequent to paying the amounts due on the Senior Series 2003A Bonds, the Prior Senior Bonds or any other Senior Bonds or other Obligations equal in priority with the Senior Series 2003A Bonds and the Prior Senior Bonds that may be issued and certain other applications, but prior to making any payment on any Senior Subordinate Obligations or on the Prior Subordinate Bonds or other Subordinate Obligations. See Appendix C, "SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS—Establishment of Accounts".



The Corporation reserves the right to deposit with the Trustee a Reserve Fund Facility in satisfaction of the Reserve Account Requirement applicable to the Senior Series 2003A Bonds upon receipt of a Rating Affirmation.

### **Withdrawal of Excess Coverage**

The General Bond Resolution provides that the Corporation may withdraw amounts from the Revenue Account, under certain circumstances, free and clear of the lien of the General Bond Resolution if, as certified to the Trustee by an Authorized Officer, there exists Excess Coverage after such withdrawal, and if the Corporation delivers a Cash Flow Projection to the Rating Agencies, as provided in the General Bond Resolution. See Appendix C, "SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS" and "—Establishment of Accounts."

### **Additional Bonds and Other Obligations**

The General Bond Resolution permits the issuance of Additional Bonds, or other Obligations, including Variable Rate Demand Bonds or Obligations, subject to certain conditions specified in the General Bond Resolution. The priority of claim as to payment of such Additional Bonds or other Obligations under the General Bond Resolution may be equal to or inferior to that of the Senior Series 2003A Bonds and the Prior Senior Bonds or may be superior or equal to that of the Prior Subordinate Bonds.

The General Bond Resolution also permits the Corporation to undertake additional Obligations pursuant to certain types of contracts ("Obligation Facilities" or "Swap Facilities"). The priority of payment of Obligation Facilities or Swap Facilities may be equal to or inferior to that of the Senior Series 2003A Bonds, the Prior Senior Bonds and any other Senior Obligations or equal to or superior to that of any Subordinate Obligations, including the Prior Subordinate Bonds.

Prior to issuing Additional Bonds or entering into Obligation Facilities or Swap Facilities, the Trustee is required to receive a Rating Affirmation from each Rating Agency maintaining a rating on the Senior Series 2003A Bonds that issuing such Additional Bonds or entering into such Obligation Facilities or Swap Facilities in and of itself will not have an adverse effect on the rating of any Outstanding Bonds.

## **CERTAIN RISK FACTORS**

Investors should consider the factors set forth below in light of the payment priorities of the Senior Series 2003A Bonds, the Prior Senior Bonds and any other Senior Obligations over the Prior Subordinate Bonds and any other Subordinate Obligations. See "SECURITY AND SOURCES OF PAYMENT FOR THE SENIOR SERIES 2003A BONDS—Additional Bonds and Other Obligations". **This section of this Official Statement does not include all risk factors, but is an attempt to summarize certain of such matters. Investors should read this Official Statement in its entirety.**

### **Certain Considerations Affecting the Receipt of Revenues in the Trust Estate**

The availability under the General Bond Resolution of adequate amounts to fund the timely payment of Obligation debt service and other expenses required to be paid thereunder is dependent upon the performance of the Student Loans to be acquired as part of the Trust Estate pledged thereunder. The Corporation currently expects to apply by July 1, 2004 all Senior Series 2003A-1 Bond proceeds initially available, along with all funds made available therefor as a result of the initial application of Senior Series 2003A-2 Bond proceeds, to finance Student Loans to the acquisition or origination of a portfolio of FFELP Loans that are guaranteed by KHEAA. See "USE OF PROCEEDS" and Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM – Legislative and Administrative Matters." The Corporation's current expectation that Revenues received with respect to the Loan portfolio will be sufficient to fund General Bond Resolution requirements, and the initial ratings assigned to the Senior Series 2003A Bonds by the Rating Agencies, is based upon cash flow projections derived from certain assumptions relative to Loan portfolio composition and performance. The Corporation believes such assumptions to be reasonable based upon its historic and current

FFELP Loan experience. There can be no assurance, however, that actual Loan portfolio results will conform to such projections. See “THE CORPORATION—The Corporation’s Education Finance and Servicing Activities”.

Revenues actually received with respect to the Loans may vary greatly in both timing and amount as a result of a variety of economic, social and other factors, including both individual factors, such as additional periods of deferral or forbearance prior to or after a borrower’s commencement of repayment, loan consolidations or refundings, and general factors, such as a general economic downturn, that could increase the amount of defaulted Loans. Because Federal Consolidation Loans are fixed rate loans, low-interest rate environments create an increased risk that borrowers may consolidate variable rate Loans. Failures by borrowers, guaranty agencies and the federal Department of Education (“Department”) to make payments with respect to Loans on a timely basis, and the incidence of borrower defaults and prepayments, will affect the amount of Revenues received by the Corporation. Congress has periodically adopted legislation, and is considering additional legislation, that provides for, among other things, interest rate caps and additional periods of deferment with respect to Loans made to members of the military, including reservists. Payments received by the Corporation on Loans made to borrowers who qualify for such relief may be subject to such limitations. There can be no assurance that additional legislation of this type will not be adopted in the future. See “THE CORPORATION—The Corporation’s Education Finance and Servicing Activities—*Student Loans Securing Student Loan Revenue Bonds*” and Appendix A, “SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Certain Recent Developments”, “—The Consolidation Loan Program” and “—Federal Insurance and Reinsurance and Reimbursement of Guaranty Agencies”.

### **Noncompliance with Certain Higher Education Act Requirements**

The provisions of the Higher Education Act applicable to FFELP Loans, and the implementing regulations thereunder, constitute a comprehensive federal program controlling the terms and conditions of FFELP Loans, including certain fees and other amounts payable by the holders thereof, the administrative requirements applicable thereto and the related duties and permitted activities of FFELP participants. Noncompliance with such requirements with respect to Loans by the Corporation or by any other entity might adversely affect payment of principal of and interest on the Bonds when due. The Department has broad powers under the Higher Education Act to assure the compliance of FFELP participants with program requirements and a failure by a participant to so comply may result in substantial penalties, including the withholding by the Department of federal payments otherwise due to such participant under the program. The Department has additional powers under the Higher Education Act with respect to guaranty agencies and their reserves, including the ability, subject to certain requirements, to terminate the activities and to transfer the reserve fund assets of such entities. There can be no assurance that the exercise by the Department of such powers will not adversely affect the interests of Owners of the Senior Series 2003A Bonds. See “THE CORPORATION – The Corporation’s Education Finance and Servicing Activities – *Servicing of FFELP Loans and Other Education Loans*”, “GUARANTY AGENCIES” and Appendix A, “SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM”. Such provisions and regulations have been the subject of extensive amendment in recent years. There can be no assurance that further amendments thereto, or that other federal legislation, will not adversely affect the interests of Owners of the Senior Series 2003A Bonds. See Appendix A, “SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Legislative and Administrative Matters” and “—Federal Direct Student Loan Program”.

The Higher Education Act and the applicable regulations thereunder require the lenders, guarantors and servicers to follow certain due diligence procedures in an effort to ensure that FFELP Loans are properly made and disbursed to, and timely repaid by, the borrowers. Such procedures are specifically set forth in the Code of Federal Regulations and certain other guidance issued by the Department, and no attempt has been made in this Official Statement to completely describe those procedures. Failure to follow such procedures with respect to Loans might result in the refusal by the Department to make reinsurance payments to a Guaranty Agency on such Loans or might result in the Guaranty Agency’s refusal to honor its guarantee on such Loans to the Corporation. Such action by the Department could adversely affect a Guaranty Agency’s ability to honor guarantee claims with respect to Loans made by the Corporation, and loss or delay in receipt of guarantee payments to the Corporation by a Guaranty Agency with respect to Loans could adversely affect the amount or timing of payment of principal of and interest on the Senior Series 2003A Bonds. See “THE CORPORATION—The Corporation’s Education Finance and Servicing

Activities—*Servicing of FFELP Loans and Other Education Loans*”, “GUARANTY AGENCIES” and Appendix A, “SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM”.

### **Basis Risk**

The interest rate for the Senior Series 2003A Bonds will initially be an Auction Rate determined in accordance with the Auction Procedures. The Loans, however, generally bear interest at an effective rate (taking into account special allowance payments authorized to be made under the Higher Education Act, or similar allowances, if any, authorized from time to time by federal law or regulations (the “Special Allowance Payments”)) (the “Loan Rates”) equal to the average bond equivalent rates of weekly auctions of 91-day Treasury bills for each quarter (the “91-day T-Bill Rate”) (or, in certain circumstances, the weekly average one-year constant maturity Treasury yield) plus margins specified for such Loans. Special Allowance Payments on FFELP Loans disbursed after January 1, 2000 are computed based upon 90-day commercial paper rates plus specified margins. See Appendix A, “SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Legislative and Administrative Matters”. As a result of these differences between the indices or methodologies used to determine the Loan Rates and the interest rates on the Senior Series 2003A Bonds, the Loan Rates applicable to some or all Loans can be expected to vary from time to time from the interest rates applicable to the Bonds.

### **Uncertainty as to Available Remedies**

If an Event of Default occurs under the Resolutions that causes Owners of Senior Obligations to fail to receive interest or principal payments when due, the Trustee is authorized, subject to certain conditions, to sell the Loans pledged thereunder. There can be no assurance, however, that the Trustee would be able to find a purchaser for such Loans in a timely manner or that the proceeds of any such sale, together with amounts then available in the Debt Service Reserve Account, would be sufficient to fund payment of the Outstanding Senior Series 2003A Bonds and accrued interest thereon. See Appendix C, “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS”.

The remedies available to Owners of the Senior Series 2003A Bonds upon an Event of Default under the Resolutions or other documents described herein are in many respects dependent upon regulatory and judicial actions that often are subject to discretion and delay. Under existing constitutional and statutory law and judicial decisions, including specifically Title 11 of the United States Code (the federal bankruptcy code), the remedies specified by the Resolutions and such other documents may not be readily available or may be limited. The various legal opinions to be delivered concurrently with the issuance of the Senior Series 2003A Bonds will be qualified, as to the enforceability of the various legal instruments, by limitations imposed by bankruptcy, reorganization, insolvency or other similar laws affecting the rights of creditors generally.

### **Reliance on Rating Affirmations**

The Resolutions provide that the Corporation and the Trustee may undertake various actions based upon receipt by the Trustee of confirmation from each Rating Agency that the outstanding rating assigned by the respective Rating Agency to the Bonds is not thereby impaired. Such actions include the execution and delivery of Additional Obligations, the inclusion in the Trust Estate of additional Student Loans that are other than as described herein, the extension of certain dates for the acquisition or origination of Student Loans, the continued origination or purchase of FFELP Loans after certain changes in the Higher Education Act, the implementation of or certain amendments to certain programs to reduce costs to Student Loan borrowers, and the acquisition or disposition of Student Loans at prices other than as described herein. To the extent such actions are taken after issuance of the Senior Series 2003A Bonds, investors in the Senior Series 2003A Bonds will be relying on the evaluation by the Rating Agencies of such actions and their impact on credit quality. Currently, the Rating Agencies rating the Bonds will be Moody’s Investors Service, Inc. (“Moody’s”) and Standard & Poor’s, a division of the McGraw-Hill Companies (“Standard & Poor’s”). Information on the ratings assigned to the Senior Series 2003A Bonds can be obtained from Moody’s at 99 Church Street, New York, New York 10007 and from Standard & Poor’s at 55 Water Street, 40<sup>th</sup> Floor, New York, New York 10007.

## DESCRIPTION OF THE SENIOR SERIES 2003A BONDS

### General

The Senior Series 2003A Bonds are being issued as Auction Rate Certificates-ARCs<sup>®</sup> (“ARCs”). The applicable Auction Rate is to be established from time to time pursuant to Auction Procedures described below under “AUCTION RATE CERTIFICATES—Interest Rates on the Senior Series 2003A Bonds”. The Senior Series 2003A Bonds are expected to be delivered, are dated and will mature as set forth on the cover page hereof. The Senior Series 2003A Bonds are issued as fully-registered bonds in denominations of \$50,000 or any integral multiple thereof (an “Authorized Denomination”). Initially, the Senior Series 2003A Bonds will only be registered in the name of Cede & Co. as nominee of DTC. See “BOOK-ENTRY SYSTEM”. Interest on the Senior Series 2003A Bonds, prior to a change in the Interest Payment Date as described below, shall be payable on November 1, 2003, and on each May 1 and November 1 thereafter until maturity or earlier redemption; provided, that if such date is not a Business Day, such interest will be payable on the next succeeding Business Day (but only for interest accrued through the preceding April 30 or October 31 as the case may be). Interest on the Senior Series 2003A Bonds is payable to the Beneficial Owners thereof according to the procedures described under “BOOK-ENTRY SYSTEM”. Principal of the Senior Series 2003A Bonds is payable upon presentation and surrender of such Bonds at the principal corporate trust office of the Trustee. The Senior Series 2003A Bonds are subject to acceleration and redemption, as described below. Further, the Series 2003A Bond Resolution provides that the Senior Series 2003A Bonds originally issued as ARCs may be converted to bear interest at a Variable Rate or a Fixed Rate, as more fully described in the Series 2003A Bond Resolution.

### Redemption Provisions

The Resolutions provide for the redemption and acceleration of the Senior Series 2003A Bonds prior to maturity, as described below. In the event that the Senior Series 2003A Bonds are to be redeemed in part, the Senior Series 2003A Bonds are to be redeemed only in the then Authorized Denominations of such Series and in such maturity or maturities thereof as the Corporation shall determine, and the Senior Series 2003A Bonds of a Series to be redeemed within a maturity are to be selected by lot or such other manner as the Trustee shall determine in accordance with the Resolutions, except as otherwise described below.

*Mandatory Redemption of Senior Series 2003A Bonds from Unexpended Bond Proceeds.* The Senior Series 2003A Bonds are subject to redemption prior to maturity by the Corporation at any time, in whole or in part, as described below, at a redemption price equal to 100% of the principal amount of such Bonds or portions thereof to be redeemed, together with accrued interest thereon to the date of redemption, from proceeds of the Senior Series 2003A Bonds deposited to the Loan Account upon the issuance thereof that have not been applied to finance Student Loans on or before July 1, 2005, unless such date is extended if a Rating Affirmation is obtained.

*Optional Redemption of Senior Series 2003A Bonds.* The Senior Series 2003A Bonds are subject to redemption prior to conversion to a Fixed Rate prior to maturity, at the option of the Corporation at any time, in whole or in part, as described below at a redemption price equal to 100% of the principal amount of such Bonds or portions thereof to be redeemed, together with accrued interest thereon to the date of redemption.

*Selection of Senior Series 2003A Bonds to be Redeemed.* Any Senior Series 2003A Bonds to be redeemed shall, except as otherwise described below, be selected by the Corporation or by the Trustee as directed by the Corporation by any one of the following means: (i) first, all Senior Bonds, second, all Senior Subordinate Bonds and, subsequently, all Subordinate Bonds of each successive next most senior Class; or (ii) in such order as the Corporation shall determine; provided, with respect to clause (ii), that either the Corporation receives a Rating Affirmation or the Trustee receives a Certificate of the Corporation to the effect that the value of the Loans (valued at par plus accrued interest and accrued special allowance payments, if any) credited to the Loan Account and all cash and Investment Securities held in the Accounts (valued at amortized value as defined for purposes of the General Bond Resolution, plus accrued interest, but excluding amounts irrevocably set aside to pay particular Obligations pursuant to the General Bond Resolution and excluding amounts on deposit in the Rebate Account and the Earnings Account), will not be less than each and all of the following sums, after giving effect to such

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<sup>®</sup> ARCs is a registered trade name of UBS PaineWebber Inc.

redemption: (a) at least 106%, of the sum of the principal of and accrued interest on all Outstanding Senior Obligations plus all accrued but unpaid Program Expenses; (b) 104% (or, subsequent to delivery to the Trustee of a Rating Affirmation addressing such change, 103%) of the sum of the principal of and accrued interest on all Outstanding Senior and Senior Subordinate Obligations plus all accrued but unpaid Program Expenses, and (c) 103% (or, subsequent to delivery to the Trustee of a Rating Affirmation addressing such change, 102%) of the sum of the principal of and accrued interest on all Outstanding Obligations plus all accrued but unpaid Program Expenses.

*Notice of Redemption of Senior Series 2003A Bonds.* The Trustee will give notice of redemption by mailing a copy of the redemption notice by first class mail, postage prepaid, to the registered owners of any Senior Series 2003A Bonds to be redeemed at the address of such owner appearing on the registration books of the Trustee. Notice of redemption will be given not more than 30 days nor less than 10 days prior to the redemption date. Such notice shall state whether the Trustee then holds sufficient moneys to fund such redemption and whether such redemption is dependent upon the issuance of refunding obligations or the deposit of funds from other sources by the Corporation. Neither failure to give such notice nor any defect therein will affect the validity of the proceedings for redemption of any Senior Series 2003A Bond not affected by such failure or defect. While the Senior Series 2003A Bonds are held by DTC or its nominee notice of redemption shall be given to DTC or its nominee. See “BOOK-ENTRY SYSTEM”.

*Effect of Redemption.* Notice having been given as aforesaid, the Senior Series 2003A Bonds called for redemption will become due and payable on the Redemption Date at the redemption price, plus accrued interest to the Redemption Date. If, on the Redemption Date, moneys for the redemption of the Senior Series 2003A Bonds to be redeemed, together with interest to the Redemption Date, are held by the Trustee or any Paying Agent so as to be available therefor on said date, interest on the Senior Series 2003A Bonds called for redemption will cease to accrue on the Redemption Date.

*Acceleration of the Senior Series 2003A Bonds.* Upon the occurrence of certain Events of Default under the Resolutions, the Senior Series 2003A Bonds may be subject to acceleration as described herein. See Appendix C, “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS”.

The Resolutions provide that nonpayment of the principal of or interest on Senior Subordinate Obligations or Subordinate Obligations occurring while there are any Senior Obligations Outstanding that are not affected by the nonpayment, shall not result in an Event of Default under the Resolutions that would give rise to a right on the part of owners of affected Obligations to accelerate the Senior Series 2003A Bonds or to exercise any other remedy. The Resolutions provide that only owners of the most senior Class of Outstanding Obligations may exercise any remedy or right of enforcement or consent to any action thereunder in the event of nonpayment of Outstanding Obligations, and requires the consent of all owners of Outstanding Obligations to exercise any right or remedy under the Resolutions for any Event of Default other than nonpayment.

*Recycling Provision.* The Resolutions permit the Corporation to use revenues received on the Student Loans for the origination or acquisition of Student Loans until July 1, 2006. After such date, no amount may be transferred from the Revenue Account to the Loan Account unless the Corporation receives a Rating Affirmation permitting the Corporation to extend the date.

### **Registration of Transfer and Exchange**

In the event that the Book-Entry System is discontinued, and subject to the procedures for the transfer or exchange of ARCs as described under “AUCTION RATE CERTIFICATES”, then upon surrender for transfer or exchange of any Senior Series 2003A Bond at the corporate trust office of the Trustee, the Corporation will execute and the Trustee will authenticate and deliver in the name of the transferee or transferees, a new Senior Series 2003A Bond of the same Series and Subseries in exchange for the Senior Series 2003A Bond being transferred or exchanged, of Authorized Denominations, of like aggregate principal amount and bearing numbers not previously assigned to such Senior Series 2003A Bonds.

The Trustee will require the payment by any owner of Senior Series 2003A Bonds requesting exchange or transfer of a sum sufficient to cover any tax, fee or other governmental charge required to be paid with respect to

such exchange or transfer. Every Senior Series 2003A Bond presented or surrendered for transfer or exchange must be duly endorsed, or be accompanied by a written instrument of transfer in form satisfactory to the Trustee, duly executed, by the owner thereof or his attorney duly authorized in writing, with signature guarantees satisfactory to the Trustee.

The Trustee is not required to transfer any Senior Series 2003A Bond (i) during a period beginning at the opening of business 15 days before any selection of Senior Series 2003A Bonds of the same Series for redemption and ending at the close of business on the day of such selection, or (ii) selected for redemption in whole or in part.

## **BOOK-ENTRY SYSTEM**

Beneficial ownership interests in the Senior Series 2003A Bonds will be available in book-entry form only. Purchases and sales by the Beneficial Owners of Senior Series 2003A Bonds can be made in denominations of \$50,000 or any integral multiple thereof. Purchasers of beneficial ownership interests in the Senior Series 2003A Bonds will not receive certificates representing their interests in the Senior Series 2003A Bonds purchased and will not be Holders under the Resolutions, except as described below.

The Depository Trust Company (“DTC”), New York, New York, will act as securities depository for the Senior Series 2003A Bonds. The Senior Series 2003A Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered certificate will be issued for each Subseries of the Senior Series 2003A Bonds, each in the respective aggregate principal amount of such Subseries, and will be deposited with DTC.

DTC, the world’s largest depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934, as amended. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com).

Purchases of Senior Series 2003A Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Senior Series 2003A Bonds on DTC’s records. The ownership interest of each actual purchaser of each Senior Series 2003A Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Senior Series 2003A Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests

in Senior Series 2003A Bonds, except in the event that use of the book-entry system for the Senior Series 2003A Bonds is discontinued.

To facilitate subsequent transfers, all Senior Series 2003A Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Senior Series 2003A Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Senior Series 2003A Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Senior Series 2003A Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to DTC. If less than all of the Senior Series 2003A Bonds within a Subseries are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such Subseries to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Senior Series 2003A Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to Issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Senior Series 2003A Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, redemption premium, if any, and interest payments on the Senior Series 2003A Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Corporation or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Trustee, or the Corporation, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, redemption premium, if any, and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Corporation or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Senior Series 2003A Bonds at any time by giving reasonable notice to the Corporation or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, certificates are required to be printed and delivered.

The Corporation may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, certificates will be printed and delivered.

The preceding information in this section "BOOK-ENTRY SYSTEM" was provided by DTC for inclusion herein, and has not been independently verified by the Corporation. No representation is made by the Corporation as to the completeness or the accuracy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof.

*Neither the Corporation nor the Trustee shall have any responsibility or obligation to any DTC Participant, any Beneficial Owner or other persons claiming a beneficial ownership interest in the Senior Series 2003A Bonds under or through DTC or any DTC Participant, with respect to: (i) the accuracy of any records maintained by DTC or any DTC Participant with respect to the beneficial ownership interest in the Senior Series 2003A Bonds; (ii) the payment by DTC or any DTC Participant of any amount in respect of the principal of and premium, if any, or*

*interest on the Senior Series 2003A Bonds to any Beneficial Owner or other person for the Senior Series 2003A Bonds; or (iii) the delivery to any Beneficial Owner of the Senior Series 2003A Bonds, or any other person, of any notice which is permitted or required to be given to owners under the Resolution. Neither the Corporation nor the Trustee shall have any responsibility with respect to obtaining consents from anyone other than the registered owners.*

No assurance can be given by the Corporation or the Trustee that DTC will distribute to the Participants or the Participants will distribute to the Beneficial Owners: (i) payment of debt service on the Senior Series 2003A Bonds paid to DTC or its nominee, as the registered owner; or (ii) any redemption or other notices, or that DTC or the DTC Participants will serve or act on a timely basis or in a manner described in this Official Statement.

## **AUCTION RATE CERTIFICATES**

### **General Terms**

The Senior Series 2003A Bonds shall be issued as ARCs, shall be dated the date of initial delivery thereof and shall mature on the dates shown on the cover of this Official Statement. Any Subseries of the Senior Series 2003A Bonds may be converted to bear interest at a Variable Rate or a Fixed Rate, as more fully described in the Series 2003A Bond Resolution. Certain capitalized terms used herein with respect to the Senior Series 2003A Bonds are defined herein or in other parts of this Official Statement, including the Appendices hereto.

After the Initial Interest Period for each Subseries of the Senior Series 2003A Bonds (as described under “—Interest Rates on the Senior Series 2003A Bonds”), the Senior Series 2003A Bonds will accrue interest at the Applicable ARCs Rate determined in the manner described herein under “—Interest Rates on the Senior Series 2003A Bonds” and in Appendix F, “AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS”.

Interest on the Senior Series 2003A Bonds initially will be payable on November 1, 2003 and on each May 1 and November 1 thereafter (subject to change as described herein) (each an “Interest Payment Date”) until the earlier of maturity or redemption. Interest on each Subseries of the Senior Series 2003A Bonds will be computed on the basis of a 365-day or 366-day year, as applicable, and actual number of days elapsed during the time such Senior Series 2003A Bonds bear interest at an Auction Rate.

### **Auction Participants**

*Existing Owners and Potential Owners.* Participants in each Auction will include: (a) “Existing Owners”, which shall mean (i) with respect to and for the purpose of dealing with the Auction Agent in connection with an Auction, any Person who is a Broker-Dealer listed in the Existing Owner Registry at the close of business on the Business Day preceding the Auction Date for such Auction, and (ii) with respect to and for the purpose of dealing with the Broker-Dealer in connection with an Auction, a Person who is a Beneficial Owner of ARCs; and (b) “Potential Owners”, which shall mean any Person, (including any Existing Owner that is (i) a Broker-Dealer when dealing with an Auction Agent and (ii) a potential Beneficial Owner when dealing with a Broker-Dealer), who may be interested in acquiring ARCs (or in the case of an Existing Owner, an additional principal amount of ARCs).

By purchasing ARCs, whether in an Auction or otherwise, each prospective purchaser of ARCs or its Broker-Dealer must agree and will be deemed to have agreed: (a) to participate in Auctions on the terms set forth in APPENDIX F hereto; (b) so long as the beneficial ownership of the ARCs is maintained in book-entry form by the Securities Depository, to sell, transfer or otherwise dispose of ARCs only pursuant to a Bid or a Sell Order (each as defined in APPENDIX F hereto) in an Auction, or to or through a Broker-Dealer, provided that, in the case of all transfers other than those pursuant to an Auction, the Existing Owner of ARCs so transferred, its agent member or its Broker-Dealer advises the Auction Agent of such transfer; and (c) to have its beneficial ownership of ARCs maintained at all times in book-entry form by the Securities Depository for the account of its Participant, which in turn will maintain records of such beneficial ownership, and to authorize such Participant to disclose to the Auction Agent such information with respect to such beneficial ownership as the Auction Agent may request.



*Auction Agent.* Deutsche Bank Trust Company Americas, New York, New York, is appointed as the initial Auction Agent for the ARCs. The Trustee is directed to enter into an Auction Agency Agreement with Deutsche Bank Trust Company Americas. Any successor Auction Agent shall be: (a) a bank or trust company duly organized under the laws of the United States of America or any state or territory thereof having its principal place of business in the Borough of Manhattan, The City of New York, or such other location as approved by the Trustee and the Market Agent in writing, and having a combined capital stock, surplus and undivided profits of at least \$25,000,000; or (b) a member of the National Association of Securities Dealers, Inc., having a capitalization of at least \$25,000,000 and, in either case, authorized by law to perform all the duties imposed upon it under the Series 2003A Bond Resolution and under the Auction Agency Agreement. The Auction Agent may resign and be discharged of the duties and obligations created by the Series 2003A Bond Resolution by giving at least 90 days' written notice to the Corporation, the Trustee and the Market Agent (30 days' written notice if the Auction Agent has not been paid its fees for more than 30 days). The Auction Agent may be removed at any time by the Trustee if the Auction Agent is an entity other than the Trustee, acting at the direction of either: (a) the Corporation or (b) the Beneficial Owners of at least 66-2/3% of the aggregate principal amount of the ARCs then outstanding by an instrument signed by the Trustee, and if by the Beneficial Owners, by an instrument signed by such Beneficial Owners or their attorneys, and filed with the Auction Agent, the Corporation and the Market Agent upon at least 90 days' notice; provided that, if required by the Market Agent, an agreement in substantially the form of the Auction Agency Agreement shall be entered into with a successor Auction Agent. If the Auction Agent and the Trustee are the same entity, the Auction Agent may be removed as described above, with the Corporation acting in lieu of the Trustee.

If the Auction Agent shall resign or be removed or be dissolved, or if the property or affairs of the Auction Agent shall be taken under the control of any state or federal court or administrative body because of bankruptcy or insolvency, or for any other reason, the Trustee at the direction of an Authorized Officer shall use its best efforts to appoint a successor Auction Agent, and the Trustee and the Corporation shall thereupon enter into an Auction Agency Agreement with such successor.

The Auction Agent is acting as agent for the Corporation in connection with Auctions. In the absence of bad faith or negligence on its part, the Auction Agent shall not be liable for any action taken, suffered or omitted or for any error of judgment made in good faith unless the Auction Agent shall have been negligent in ascertaining (or failing to ascertain) the pertinent facts necessary to make such judgment.

*Broker-Dealer.* Existing Owners and Potential Owners may participate in Auctions only by submitting orders (in the manner described below) through a "Broker-Dealer", including UBS PaineWebber Inc. as the sole initial Broker-Dealer, any other broker or dealer (each as defined in the Securities Exchange Act of 1934, as amended), commercial bank or other entity permitted by law to perform the functions required of a Broker-Dealer set forth below that (a) is a "Participant" (i.e., a member of, or participant in, DTC or any successor securities depository) or an affiliate of a Participant, (b) has been selected by the Corporation with the approval of the Market Agent, and (c) has entered into a Broker-Dealer Agreement with the Auction Agent that remains effective, in which the Broker-Dealer agrees to participate in Auctions as described in the Auction Procedures, as from time to time amended or supplemented.

*Market Agent.* The "Market Agent", initially UBS PaineWebber Inc., acting pursuant to the Market Agent Agreement with the Corporation and in connection with the ARCs, shall act solely as agent of the Corporation and shall not assume any obligation or relationship of agency or trust for or with any of the Beneficial Owners.

## **Interest Rates on the Senior Series 2003A Bonds**

*Interest Payments.* Interest on the ARCs shall accrue for each Interest Period and shall be payable in arrears on each succeeding Interest Payment Date. An "Interest Period" means, with respect to ARCs, (a) so long as interest is payable on May 1 and November 1 with respect thereto and unless otherwise changed as described under "—Changes in Auction Periods, Auction Dates, or Interest Payment Dates—*Changes in Auction Period or Periods*", the Initial Interest Period and each successive period of generally 35 days thereafter, respectively, commencing on a Friday (or the Business Day following the last day of the prior Interest Period, if the prior Interest Period does not end on a Thursday) and ending on (and including) a Thursday (unless such Thursday is not followed by a Business Day, in which case on the next succeeding day that is followed by a Business Day), and (b) if, and for so long as, Interest Payment Dates are specified to occur at the end of each Auction Period, as described under "—Changes in

Auction Periods, Auction Dates, or Interest Payment Dates—*Changes in Auction Period or Periods*”, each period commencing on an Interest Payment Date and ending on, but excluding, the next succeeding Interest Payment Date. An “Interest Payment Date” for each Subseries of the Senior Series 2003A Bonds, while the Senior Series 2003A Bonds are outstanding as ARCs, means May 1 and November 1, and at maturity or earlier redemption, commencing November 1, 2003, or if any such date is not a Business Day, the next succeeding Business Day (but only for interest accrued through the preceding last day of April or October, as the case may be).

The amount of interest distributable to holders of ARCs in respect of each \$50,000 in principal amount thereof for any Interest Period or part thereof shall be calculated by the Trustee by applying the Applicable ARCs Rate for such Interest Period or part thereof to the principal amount of \$50,000, multiplying such product by the actual number of days in the Interest Period or part thereof, divided by 365 or 366, as applicable, and truncating the resultant figure to the nearest cent. Interest on the ARCs shall be computed by the Trustee on the basis of a 365-day year for the number of days actually elapsed; except that for any such calculation with respect to an Interest Payment Date occurring after January 1 of any leap year through December 31 of such leap year, such interest (for any day occurring during such period) shall be computed on the basis of a 366-day year period. The Trustee shall make the calculation described above not later than the close of business on each Auction Date upon receipt of the relevant information from the Auction Agent.

Interest payments on the ARCs are to be made by the Trustee to the persons who are registered owners of the ARCs, as of the Record Date preceding each Interest Payment Date. The ARCs are to be initially registered in the name of Cede & Co., as nominee of DTC, which is acting as the depository for the ARCs. See “BOOK-ENTRY SYSTEM” for a description of how DTC, as registered owner, is expected to disburse such payments to the Beneficial Owners.

*Applicable ARCs Rate.* For a period beginning on the Closing Date and continuing through July 6, 2003 with respect to the Senior Series 2003A-1 Bonds and through July 10, 2003 with respect to the Senior Series 2003A-2 Bonds, the Senior Series 2003A Bonds will bear interest at rates to be determined shortly before their issuance. The rate of interest on the ARCs for each Interest Period subsequent to the Initial Interest Period, to but not including the Fixed Rate Conversion Date or the Variable Rate Conversion Date, if any, shall be equal to the annual rate of interest that results from implementation of the Auction Procedures described in Appendix F, “AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS” (the “Auction Rate”), unless the Auction Rate exceeds the Maximum Rate, in which case the rate of interest on the ARCs for such Interest Period shall be the Maximum Rate, or unless the Maximum Rate shall actually be lower than the All Hold Rate, in which case the rate of interest on the ARCs for such Interest Period shall be the Maximum Rate; provided that if, on any Auction Date, an Auction is not held for any reason, then the rate of interest for the next succeeding Interest Period shall equal the Maximum Rate on such Auction Date; provided further, however, that if an Auction is scheduled to occur for the next Interest Period on a date that was reasonably expected to be a Business Day, but such Auction does not occur because such date is later not considered to be a Business Day, the Auction shall nevertheless be deemed to have occurred, and the applicable Auction Rate in effect for the next Interest Period will be the Auction Rate in effect for the preceding Interest Period and such Interest Period will generally be 35 days in duration, beginning on the calendar day following the date of the deemed Auction and ending on (and including) the applicable Auction Date (unless such date is not followed by a Business Day, in which case on the next succeeding day that is followed by a Business Day). If the preceding Interest Period was other than 35 days in duration, the Auction Rate for the deemed Auction will instead be the rate of interest determined by the Market Agent on the basis of equivalently rated auction securities with a comparable length of auction period. Notwithstanding the foregoing: (a) if the ownership of the ARCs is no longer maintained in book-entry form, the rate of interest on the ARCs for any Interest Period commencing after the delivery of certificates representing ARCs as described above shall equal the Maximum Rate on the Business Day immediately preceding the first day of such Interest Period; (b) if a Payment Default occurs, Auctions will be suspended and the Applicable ARCs Rate (as defined below) for the Interest Period commencing on or after such Payment Default and for each Interest Period thereafter to and including the Interest Period, if any, during which, or commencing less than two Business Days after, such Payment Default is cured, will equal the Default Rate; or (c) if a proposed conversion to a Fixed Rate or Variable Rate shall have failed, as described under “—Inadequate Funds for Tenders; Failed Conversion”, and the next succeeding Auction Date shall be two or fewer Business Days after (or on) any such failed Fixed Rate Conversion Date or Variable Rate Conversion Date, then an Auction shall not be held on such Auction Date and the rate of interest on the ARCs subject to the failed conversion

for the next succeeding Interest Period shall be equal to the Maximum Rate calculated as of the first Business Day of such Interest Period.

The rate per annum at which interest is payable on the ARCs for any Interest Period is herein referred to as the “Applicable ARCs Rate”. Notwithstanding anything herein to the contrary, the Applicable ARCs Rate cannot exceed the Maximum Interest Rate.

Notwithstanding anything herein to the contrary, if any ARCs or portion thereof have been selected for redemption during the next succeeding Interest Period, such ARCs or portion thereof, will not be included in the Auction preceding such redemption date, and will continue to bear interest until the redemption date at the rate established for the Interest Period prior to said Auction.

## **Auctions**

Prior to a Fixed Rate Conversion Date or a Variable Rate Conversion Date, Auctions to establish the Applicable ARCs Rate are to be held on each Auction Date, except as described under “—Interest Rates on the Senior Series 2003A Bonds—*Applicable ARCs Rate*”, by application of the Auction Procedures described in Appendix F, “AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS”. “Auction Date” shall mean initially with respect to the Senior Series 2003A-1 Bonds outstanding as ARCs, July 3, 2003, with respect to the Senior Series 2003A-2 Bonds outstanding as ARCs, July 10, 2003, and thereafter, the Business Day immediately preceding the first day of each related Auction Period, other than: (a) each Auction Period commencing after the ownership of the ARCs is no longer maintained in book-entry form, (b) each Auction Period commencing after the occurrence and during the continuance of a Payment Default; or (c) any Auction Period commencing less than the Applicable Number of Business Days after the cure or waiver of a Payment Default. Notwithstanding the foregoing, the Auction Date for one or more Auction Periods may be changed as described under “—Changes in Auction Periods, Auction Dates, or Interest Payment Dates—*Changes in Auction Period or Periods*”.

The Auction Agent shall determine the Maximum Rate, the Maximum Interest Rate, and the All Hold Rate on each Auction Date. Upon receipt of notice from the Trustee of a failed Fixed Rate conversion or Variable Rate conversion as described under “—Inadequate Funds for Tenders; Failed Conversion”, and if the next succeeding Auction Date shall be two or fewer Business Days after (or on) the failed Fixed Rate Conversion Date or Variable Rate Conversion Date, the Auction Agent shall not hold an Auction on such Auction Date, but shall calculate the Maximum Rate as of the first Business Day of the next succeeding Interest Period and give notice thereof as provided, and to the parties specified, in the Auction Agency Agreement. If the ownership of the ARCs is no longer maintained in book-entry form by the Securities Depository, the Trustee shall calculate the Maximum Rate on the Business Day immediately preceding the first day of each Interest Period commencing after delivery of certificates representing the ARCs. If a Payment Default shall have occurred, the Trustee shall calculate the Default Rate on the first day of (a) each Interest Period commencing after the occurrence and during the continuance of such Payment Default and (b) any Interest Period commencing less than the Applicable Number of Business Days after the cure of any Payment Default. The Auction Agent shall determine the “AA” Financial Commercial Paper Rate for each Interest Period other than the Initial Interest Period; *provided*, that if the ownership of the ARCs is no longer maintained in book-entry form, or if a Payment Default has occurred, then the Trustee shall determine the “AA” Financial Commercial Paper Rate for each such Interest Period. The determination by the Trustee or the Auction Agent, as the case may be, of the “AA” Financial Commercial Paper Rate shall (in the absence of manifest error) be final and binding upon the Bondholders and all other parties. If calculated or determined by the Auction Agent, the Auction Agent shall promptly advise the Trustee of the “AA” Financial Commercial Paper Rate.

So long as the ownership of the ARCs is maintained in book-entry form by the Securities Depository, an Existing Owner may sell, transfer or otherwise dispose of ARCs only pursuant to a Bid or Sell Order (as defined in Appendix F, “AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS”) placed in an Auction, or through a Broker-Dealer, *provided* that, in the case of all transfers other than pursuant to Auctions, such Existing Owner, its Broker-Dealer or its Participant advises the Auction Agent of such transfer. Prior to a Fixed Rate Conversion Date or a Variable Rate Conversion Date, Auctions shall be conducted on each Auction Date, if there is an Auction Agent on such Auction Date, in the manner described in Appendix F, “AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS”. A description of the Settlement Procedures to be used with respect to

Auctions is contained in Appendix G, "SETTLEMENT PROCEDURES FOR THE SENIOR SERIES 2003A BONDS".

### **Adjustment in Percentages**

The Market Agent shall adjust the percentage used in determining the All Hold Rate, the Applicable Percentage used in determining the Maximum Rate and the Applicable Percentage of the Kenny Index used in determining the Default Rate, if any such adjustment is necessary, in the judgment of the Market Agent, to reflect any Change of Preference Law such that ARCs paying the Maximum Rate, ARCs paying the All Hold Rate and ARCs paying the Default Rate shall respectively have equal market values before and after such Change of Preference Law. Prior to any such adjustment, the Corporation shall give notice thereof to any Rating Agencies then rating the ARCs, and no such adjustment shall be made unless such adjustment will not adversely affect the rating on any of the Senior Series 2003A Bonds or on any of the other Bonds issued pursuant to the General Bond Resolution. In making any such adjustment, the Market Agent shall take the following factors, as in existence both before and after such Change of Preference Law, into account: (a) short-term taxable and tax-exempt market rates and indices of such short-term rates; (b) the market supply and demand for short-term tax-exempt securities; (c) yield curves for short-term and long-term tax-exempt securities or obligations having a credit rating that is comparable to the ARCs; (d) general economic conditions; and (e) economic and financial factors present in the securities industry that may affect or that may be relevant to the ARCs.

The Market Agent shall effectuate an adjustment in the percentage used in determining the All Hold Rate, the Applicable Percentage used in determining the Maximum Rate and the Applicable Percentage of the Kenny Index used to determine the Default Rate by delivering written notice to the Corporation, the Trustee and the Auction Agent at least 10 days prior to the Auction Date on which the Market Agent desires to effect such change. Such notice shall be effective only if it is accompanied by a Favorable Opinion.

### **Changes in Auction Periods, Auction Dates, or Interest Payment Dates**

*Changes in Auction Period or Periods.* While any Senior Series 2003A Bonds are outstanding as ARCs, the Market Agent may change, upon meeting certain conditions, including receipt of a Favorable Opinion, the length of one or more Auction Periods; provided, however, that any such changed Auction Period shall not be less than seven days unless the Corporation has given its prior written consent to such shorter period. In connection with any such change, or otherwise, the Market Agent may, upon receipt of a Favorable Opinion, change Interest Payment Dates. Any change in the length of the Auction Period requires the written consent of an Authorized Officer and must be made for the purpose of conforming to current market practice with respect to certain securities.

The change in the length of one or more Auction Periods shall not be allowed unless Sufficient Clearing Bids (as defined in Appendix F, "AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS") existed at both the Auction before the date on which the notice of the proposed change was given and the Auction immediately preceding the proposed change. Such change shall take effect only if certain requirements are met as described in the Series 2003A Bond Resolution.

*Changes in the Auction Date.* While any of the Senior Series 2003A Bonds are outstanding as ARCs, the Market Agent:

- (a) to conform with then-current market practice with respect to similar securities, shall, and
- (b) to accommodate economic and financial factors that may affect or be relevant to the day of the week constituting an Auction Date and the interest rate borne on the ARCs and upon receipt of a Favorable Opinion and with the written consent of an Authorized Officer, may

specify an earlier Auction Date (but in no event more than five Business Days earlier) than the Auction Date that would otherwise be determined in accordance with the definition of "Auction Date" with respect to one or more specified Auction Periods. The Authorized Officer shall not consent to such change in the Auction Date, if such consent is required as described above, unless he or she shall have received from the Market Agent, not less than three days nor more than 20 days prior to the effective date of such change, a written request for consent together

with a certificate demonstrating the need for change in reliance on such factors. The Market Agent shall provide notice of any determination to specify an earlier Auction Date for one or more Auction Periods by means of a written notice delivered at least ten days prior to the proposed changed Auction Date to the Trustee, the Auction Agent, the Corporation and the Securities Depository.

In connection with any change in the Auction terms described above, the Auction Agent shall provide such further notice to such parties as is specified in the Auction Agency Agreement.

No change shall be made to the Auction Period or Auction Date unless the Corporation and the Trustee shall have received confirmation from each Rating Agency then rating any of the Senior Series 2003A Bonds or the other Bonds issued pursuant to the General Bond Resolution that the ratings on any of such Bonds will not be adversely affected thereby.

*Changes in the Interest Payment Dates.* The Market Agent:

- (a) to conform with then-current market practice with respect to similar securities, shall, and
- (b) to accommodate economic and financial factors that may affect or be relevant to the Interest Payment Date and the interest rate borne by the ARCs and with the written consent of an Authorized Officer, may

change the Interest Payment Date with respect to the ARCs to or from semi-annual payments on May 1 and November 1 of each year to or from the Interest Payment Dates specified in the notice of such change.

The changes in Auction terms described above must be made with respect to all of the ARCs of a Series. In connection with any change in Auction terms described above, the Auction Agent will provide such further notice to such parties as is specified in the Auction Agency Agreement.

### **Disruption in Auction Procedures**

If an Auction with respect to the Senior Series 2003A Bonds outstanding as ARCs is scheduled to occur for the succeeding Interest Period on a day that was reasonably expected to be a Business Day, but such Auction does not occur because such date is later not considered to be a Business Day, the Auction shall, nevertheless be deemed to have occurred, and the applicable Auction Rate in effect for the next Interest Period will be the Auction Rate in effect for the preceding Interest Period and such Interest Period will generally be 35 days in duration, beginning on the calendar day following the date of the deemed Auction and ending on (and including) the applicable Auction Date (unless that Auction Date is not followed by a Business Day, in which case on the next succeeding day that is followed by a Business Day). If the preceding Interest Period was other than generally 35 days in duration, the Auction Rate for the deemed Auction will instead be the rate of interest determined by the Market Agent on equivalently rated auction securities with a comparable length of auction period.

### **Fixed Rate Conversion of ARCs**

All, but not less than all, of any series of the ARCs may be converted to bear interest at a Fixed Rate to their final maturity by the Corporation. If any series of the ARCs is to be converted to bear interest at a Fixed Rate, a Fixed Rate Conversion Date for such series of ARCs shall be specified.

Not later than the 15th day preceding the Fixed Rate Conversion Date, notice of the conversion shall be given by first class mail by the Trustee to the Auction Agent and the Owners of all ARCs of such series, and that series of the Senior Series 2003A Bonds will be subject to mandatory tender as described below under “—Mandatory Tender of ARCs upon Conversion; Certain Notices”.

No such conversion shall occur unless the Corporation has received a Rating Affirmation with respect to the rating on any of the Bonds (other than the Series 2003A Bonds being converted) outstanding under the General Bond Resolution. In the event that the Corporation determines that the conversion to a Fixed Rate will not occur on

a scheduled Fixed Rate Conversion Date, the Market Agent may schedule a new Auction Date for the series of ARCs as to which the conversion was to take place as provided in the Series 2003A Bond Resolution.

### **Variable Rate Conversion of ARCs**

All, but not less than all, of any series of the ARCs may be converted to bear interest at a Variable Rate by the Corporation. If any series of the ARCs is to be converted to bear interest at a Variable Rate, a Variable Rate Conversion Date for such series of the ARCs shall be specified.

Not later than the 15th day preceding the Variable Rate Conversion Date, notice of the conversion shall be given by first class mail by the Trustee to the Auction Agent and the Owners of all ARCs of such series, and that series of the Senior Series 2003A Bonds will be subject to mandatory tender as described below under “—Mandatory Tender of ARCs Upon Conversion; Certain Notices”.

No such conversion shall occur unless the Corporation has received a Rating Affirmation with respect to the rating on any of the Bonds (other than the Series 2003A Bonds being converted) outstanding under the General Bond Resolution. In the event that the Corporation determines that the conversion to a Variable Rate will not occur on a scheduled Variable Rate Conversion Date, the Market Agent may schedule a new Auction Date for the series of ARCs as to which the conversion was to take place as provided in the Series 2003A Bond Resolution.

### **Mandatory Tender Upon Conversion; Certain Notices**

*Mandatory Tender Upon Conversion.* Any series of the Senior Series 2003A Bonds to be converted to bear interest at a Fixed Rate or a Variable Rate shall be subject to mandatory tender for purchase on the Fixed Rate Conversion Date or Variable Rate Conversion Date, at a price equal to the principal amount thereof plus accrued interest, if any, to the Fixed Rate Conversion Date or Variable Rate Conversion Date.

*Notice to Registered Holders.* Any notice of conversion given to Holders as described above under “—Fixed Rate Conversion of ARCs” or “—Variable Rate Conversion of ARCs” shall, in addition to the requirements described therein, specify that all Outstanding Senior Series 2003A Bonds of such series subject to such conversion are subject to mandatory tender pursuant to the provisions thereof and of the Series 2003A Bond Resolution and will be purchased on the Fixed Rate Conversion Date or the Variable Rate Conversion Date by payment of a purchase price equal to the principal amount thereof plus accrued interest, if any, to the Fixed Rate Conversion Date or the Variable Rate Conversion Date.

*Payment of Purchase Price by Trustee.* On any Fixed Rate Conversion Date or Variable Rate Conversion Date, the Trustee shall pay the purchase price of the series of Senior Series 2003A Bonds required to be tendered for purchase, surrendered as described below properly endorsed for transfer in blank with all signatures guaranteed, to the selling Holders thereof on or before 3:00 P.M. Such payments shall be made in immediately available funds to any Person other than the Corporation, but solely from moneys representing proceeds of the remarketing of the Senior Series 2003A Bonds of such series, and neither the Corporation, the Trustee, the Paying Agent nor the Remarketing Agent shall have any obligation to use funds from any other source.

*Delivery of Senior Series 2003A Bonds; Effect of Failure to Surrender Bonds.* The Senior Series 2003A Bonds to be purchased on any Fixed Rate Conversion Date or Variable Rate Conversion Date shall be required to be delivered to the designated office of the Trustee or its designated agent for such purposes, at or before 12:00 Noon on such date. If the Holder of any Senior Series 2003A Bond that is subject to purchase as described herein fails to deliver such Senior Series 2003A Bond to the Trustee, or its designated agent for such purposes, for purchase on the purchase date, and if the Trustee, or its designated agent for such purposes, is in receipt of the purchase price therefor, such Senior Series 2003A Bond shall nevertheless be deemed tendered and purchased on the Fixed Rate Conversion Date or the Variable Rate Conversion Date and shall be an Undelivered Bond as described below under “—Undelivered Bonds” and registration of the ownership of such Senior Series 2003A Bond shall be transferred to the purchaser thereof as described below under “—Undelivered Bonds”. The Trustee shall, as to any Undelivered Bonds, (a) promptly notify the Remarketing Agent, the Auction Agent, the Paying Agent and the Registrar of such non-delivery and (b) the Registrar shall place a stop transfer against an appropriate amount of Senior Series 2003A Bonds subject to conversion registered in the name of the Holder(s) on the Bond Register. The Registrar shall place

such stop transfer(s) on Senior Series 2003A Bonds subject to conversion registered in the name of such Holder(s) (until stop transfers have been placed against an appropriate amount of Senior Series 2003A Bonds of the appropriate series) until the appropriate tendered Senior Series 2003A Bonds are delivered to the Trustee or its designated agent. Upon such delivery, the Registrar shall make any necessary adjustments to the Bond Register. Pending delivery of such tendered Senior Series 2003A Bonds, the Trustee, or its designated agent, shall hold the purchase price therefor uninvested in a segregated subaccount for the benefit of such Holder(s).

### **Inadequate Funds for Tenders; Failed Conversion**

If the funds available for the purchase of Senior Series 2003A Bonds are inadequate for the purchase of all Senior Series 2003A Bonds required to be tendered on any Fixed Rate Conversion Date or Variable Rate Conversion Date or if a proposed conversion to a Fixed Rate or Variable Rate otherwise fails as described above, the Trustee shall: (a) return all tendered Senior Series 2003A Bonds to the Owners thereof; (b) return all moneys received for the purchase of such Senior Series 2003A Bonds to the persons providing such moneys; and (c) notify the Corporation, the Auction Agent, the Remarketing Agent and the Paying Agent of the return of such Senior Series 2003A Bonds and moneys and the failure to make payment for tendered Senior Series 2003A Bonds. After any such failed conversion, the Senior Series 2003A Bonds subject to the failed conversion shall remain outstanding as ARCs. Auctions shall be conducted beginning on the first Auction Date occurring more than two Business Days after the failed Fixed Rate Conversion Date or Variable Rate Conversion Date, and interest payable thereon shall be determined and paid according to the Series 2003A Bond Resolution.

### **No Tender Purchases After Call for Redemption**

Senior Series 2003A Bonds (or portions thereof) called for redemption shall not be subject to tender and purchase on a subsequent Fixed Rate Conversion Date or a Variable Rate Conversion Date.

### **Undelivered Bonds**

Any Bonds that are required to be tendered on a Fixed Rate Conversion Date or Variable Rate Conversion Date and that are not delivered on such date, and for the payment of which there has been irrevocably held in trust in a segregated subaccount for the benefit of such Owner an amount of money sufficient to pay the purchase price, including any accrued interest due to (but not after) such purchase date with respect to such Bonds, shall be deemed to have been purchased, and shall be Undelivered Bonds. In the event of a failure by a Bondholder to tender its Bonds on or prior to the required date, such non-delivering Bondholder of such Undelivered Bonds shall not be entitled to any payment other than the purchase price due on the purchase date and such Undelivered Bonds in the hands of such non-delivering Bondholder shall no longer accrue interest or be entitled to the benefits of the General Bond Resolution, except for the payment of the purchase price due on the purchase date; *provided, however*, that the indebtedness represented by such Bonds shall not be extinguished, and the Paying Agent and Registrar shall transfer, authenticate and deliver such Bonds as provided in the Series 2003A Bond Resolution. The Paying Agent shall give telephonic notice to the Trustee and the Registrar, promptly confirmed by mail of all Undelivered Bonds.

## **THE CORPORATION**

The General Assembly of the Commonwealth established the Corporation in 1978 to provide a program of financing, making and purchasing insured student loans in the Commonwealth.

### **Governance and Functions**

The Corporation is an independent *de jure* municipal corporation and political subdivision of the Commonwealth. The Corporation is authorized by the Act: (a) to make, purchase and sell, and to participate in the making, purchasing and selling of insured student loans; (b) to collect and pay reasonable fees and charges in connection with its making, purchasing, selling and servicing of insured student loans; (c) to procure insurance in respect of all insured student loans made or purchased by it; (d) to make, execute, and effectuate agreements with any federal or state agency, person, or entity necessary to accomplish its corporate purposes; (e) to accept and

comply with the conditions of any appropriations, loans, grants, and other aid to the Corporation; (f) to invest its funds not required for immediate disbursement; (g) to issue its notes and bonds for the purpose of carrying out its corporate powers and duties; and (h) to service and collect educational loans for other lenders, holders and educational institutions.

The term “insured student loans” is currently defined for purposes of the Act to include loans to students who are qualified under the federal Higher Education Act of 1965, as amended, on which the payment of principal and interest is at least ninety-five percent insured by a guaranty agency and reinsured by the Secretary in accordance with the Higher Education Act or at least ninety-five percent insured as to principal amount by the federal government under the Higher Education Act or the Health Professions Educational Assistance Act of 1976, as amended.

The Corporation is governed by its Board of Directors, which may officially act by a majority of its members. On July 18, 2002, the Governor of the Commonwealth issued an executive order, 2002-848, expanding the number of members of the Corporation’s Board of Directors through the addition of eight voting members, of whom six are to be public members of KHEAA’s Board of Directors. The remaining such additional members are to be the Treasurer of the Commonwealth and the President of the Association of Independent Kentucky Colleges and Universities. In addition, the executive order provided that the President of the Council on Postsecondary Education would serve as an ex-officio member of the Board of Directors in substitution for the Chairman of the Council on Postsecondary Education. The provisions of the Act addressing the composition of the Corporation’s Board of Directors were amended to provide that all current individual members of the Corporation’s Board of Directors shall also be members of the KHEAA’s Board of Directors, effective June 24, 2003, through operation of Senate Bill No. 17 as enacted by the 2003 Regular Session of the General Assembly of the Commonwealth. The Board of Directors consists of nineteen members, of whom fourteen are appointed by the Governor from the general public residing in the Commonwealth to serve a term of four years each and five serve *ex officio* by reason of their positions as Treasurer of the Commonwealth, President of the Council on Postsecondary Education of the Commonwealth, Secretary of the Finance and Administration Cabinet of the Commonwealth, President of the Association of Independent Colleges and Universities and Commissioner of Education. The Board of Directors elects from its membership a Chairman and Secretary-Treasurer.

The Corporation’s current Chairman, Secretary-Treasurer and other Directors are set forth below. Three positions are currently vacant.

#### Board of Directors of the Corporation

##### Name of Director

##### Principal Occupation

Joey B. Bailey

Executive Vice President, Chief Financial  
Officer and Treasurer  
Presbyterian Church (U.S.A.)  
Louisville, Kentucky

Marcia Kuegel Carpenter

Guidance Counselor  
Daviess County Public Schools  
Owensboro, Kentucky

Austin B. Carroll  
Chairman

General Manager  
Hopkinsville Electric System  
Hopkinsville, Kentucky

Betty Young Farris

Student Advocate and Retired School  
Administrator  
Bowling Green Independent Schools  
Roundhill, Kentucky



Janis G. Garr	Human Resource Manager Ashland, Inc. Lexington, Kentucky
Ronald L. Green	Project Director Louisville Minority Development Center Louisville, Kentucky
Shirley A. Huelsmann	Homemaker and Civic Leader Fort Mitchell, Kentucky
Jim A. Jackson Secretary-Treasurer	Retired Frankfort, Kentucky
Albert A. Kirkpatrick	Retired Louisville, Kentucky
Bobbie D. Powell	Former Labor Representative American Federation of State, County and Municipal Employees Louisville, Kentucky
John G. Prather, Jr.	Attorney at Law Somerset, Kentucky
Mary Jo Young	Banking and Civic Activist Elizabethtown, Kentucky
Gary S. Cox ( <i>ex officio</i> )	President Association of Independent Colleges & Universities Frankfort, Kentucky
Gordon C. Duke ( <i>ex officio</i> )	Secretary, Finance and Administration Cabinet, Commonwealth of Kentucky Frankfort, Kentucky
Jonathan Miller ( <i>ex officio</i> )	State Treasurer Office of the Kentucky State Treasurer Frankfort, Kentucky
Dr. Thomas Layzell ( <i>ex officio</i> )	President Council on Postsecondary Education Frankfort, Kentucky
Gene Wilhoit ( <i>ex officio</i> ) (effective June 24, 2003)	Commissioner Kentucky Department of Education Frankfort, Kentucky

The Corporation's bylaws provide that officers of its Board of Directors serve until replaced.

The Corporation currently has a staff of approximately 216 full-time equivalent employees. Its principal office is located at 10180 Linn Station Road, Post Office Box 24266, Louisville, Kentucky, 40224-0266, telephone number (502) 329-7079, website [www.studentloanpeople.com](http://www.studentloanpeople.com).

## **Principal Management Personnel**

Principal management personnel involved in the Corporation's Education Finance and Servicing Activities are as follows:

Joe L. McCormick, Executive Director and Chief Executive Officer, has overall management responsibility for the Corporation. Dr. McCormick also serves as Executive Director of KHEAA. Prior to this appointment in 2001, Dr. McCormick had 23 years of experience in student financial aid, including 12 years serving as President and Chief Executive Officer of the Texas Guaranteed Student Loan Corporation and four years with the United States Department of Education in Washington, D.C. Dr. McCormick is a member of the Federal Executive Institute. He holds a B.A. in Political Science from West Texas State University, a Master's Degree in Political Science from Mississippi State University and a Doctor of Philosophy in Education Policy and Training from the University of Texas at Austin.

Roger B. Tharp, President and Chief Operating Officer, has overall responsibility for operations of the Corporation. Before this appointment in 1993, he was Director of the Division of Program Administration for KHEAA for nineteen years. He has served as Secretary for the National Council on Higher Education Loan Programs and served on its Servicing Committee. He is also a member of the Student Loan Servicing Alliance and currently serves on its Board of Directors. His previous employment includes six combined years of financial aid management experience at the United Electronics Institute and the University of Louisville, and one year in credit management for Sears, Roebuck and Company. Mr. Tharp holds an M.B.A. from the University of Louisville and a B.S. degree in Business and Economics from the University of Kentucky.

Charles J. Robinson, CPA, Chief Financial Officer, has responsibility for all financial and human resource matters for both KHEAA and the Corporation. Mr. Robinson joined the Corporation in October 2002. He has over 14 years student loan experience. Mr. Robinson worked for another student loan company prior to his current post. He graduated from West Texas State University with a double major in accounting and finance.

Richard Casey, General Counsel to KHEAA and the Corporation, provides legal services to both organizations. Mr. Casey joined KHEAA and the Corporation as General Counsel in 1978. He holds a J.D. degree from the University of Louisville and a B.S. degree in political science from Centre College of Kentucky.

Sherry M. Cooper, Senior Vice President-Corporate Counsel, is responsible for general legal and contractual compliance activities. Ms. Cooper joined the Corporation in April 1997, after serving as an attorney with the Kentucky Department of Insurance. Her previous employment also includes serving an appointment on the Kentucky Health Policy Board, two years in the private practice of law, and four years with Legal Services. Since 1998, Ms. Cooper has served on the NCHELP Regulation Committee and has participated in the NCHELP Legal Committee. Ms. Cooper holds a J.D. from Chase College of Law, Northern Kentucky University, and a B.A. in Elementary Education from the College of the Ozarks, Missouri.

Mary C. Henry, Senior Vice President-Operations, is responsible for customer service, loan administration and operational support. Ms. Henry joined the Corporation in 1994 and previously served as Vice President, Information Systems. Her prior employment includes fifteen years with Liberty National Bank & Trust Company, where she served as Vice President of Student and Retirement Services. Ms. Henry is a graduate of Bellarmine College, Louisville, with an M.B.A., and a graduate of the University of Louisville, with a B.S. in Commerce.

Kathleen B. Vogt, Vice President-Finance, is responsible for financial management, financial services and administrative services. Before joining the Corporation in 1997, she served five years as Director of Audit for the Kentucky Housing Corporation. Prior to that, Ms. Vogt was employed by Deloitte and Touche. Ms. Vogt is a Certified Public Accountant and holds an M.B.A. from the University of Louisville and a B.A. in Accounting from Bellarmine College, Louisville.

## **The Corporation's Education Finance and Servicing Activities**

*General.* The Corporation's Education Finance and Servicing Activities currently include: (i) the origination and secondary market acquisition of education loans originated pursuant to the Federal Family Education

Loan Program (“FFELP Loans”) and the federal Health Education Assistance Loan Program (“HEAL Loans”); (ii) the financing of FFELP Loans; and (iii) the servicing of FFELP Loans and of other education loans.

The Corporation’s statutory authority to finance education loans other than Student Loans was clarified, effective June 24, 2003, through operation of Senate Bill No. 130 as enacted by the 2003 Regular Session of the General Assembly of the Commonwealth. The Corporation is not currently authorized to finance such loans through application of Bonds that are secured under the General Bond Resolution. The Corporation reserves the right to expand its Education Finance Activities to include the origination, acquisition and financing of other education loans, subject to compliance with applicable law and contractual requirements. The Senior Series 2003A Bonds are being issued for the purpose of providing funds for the financing, or refinancing, of FFELP Loans. The General Bond Resolution conditions the expenditure of funds that are credited to the Loan Account to finance education loans other than FFELP Loans upon receipt of a Rating Affirmation.

*FFELP Loan Origination and Acquisition.* The Corporation is an eligible lender for purposes of the Federal Family Education Loan Program and originates FFELP Loans both for its own account and on behalf of other eligible lenders. Certain origination functions are performed for the Corporation by KHEAA. In addition, the Corporation acquires FFELP Loans from other eligible lenders, both pursuant to ongoing contractual obligations and on a transactional basis. Ninety-three (93) lending institutions currently refer loan applications to the Corporation for origination and three lending institutions currently participate in the secondary market program.

*FFELP Loan Financing.* The Corporation has heretofore issued several series of its Insured Student Loan Revenue Bonds, of which \$152,275,000 remained outstanding as of March 31, 2003 (the “Insured Student Loan Revenue Bonds”) pursuant to the 1983 Resolution. The Insured Student Loan Revenue Bonds are secured as provided by the 1983 Resolution and are not secured by the General Bond Resolution, or by any interest in the Trust Estate pledged under the General Bond Resolution to the payment of the Senior Series 2003A Bonds. Prior to 1997, all FFELP Loans acquired by the Corporation were financed through application of proceeds of Insured Student Loan Revenue Bonds. The 1983 Resolution permits the application of funds held thereunder to finance FFELP Loans that are guaranteed by KHEAA or insured directly by the Secretary of Education and HEAL Loans.

The Corporation currently has in effect a line of credit agreement (the “Line of Credit”) pursuant to which it may receive advances from time to time in an aggregate outstanding principal amount of up to \$100,000,000. Payment obligations of the Corporation arising from advances pursuant to the Line of Credit are limited as to recourse to the trust estate established pursuant to a Line of Credit Trust Agreement.

Neither the Insured Student Loan Revenue Bonds nor the Line of Credit are payable from Loans or other assets included in the Trust Estate established under the General Bond Resolution. No education loan or other asset pledged under the 1983 Resolution or under the Line of Credit Trust Agreement is pledged to secure or expected to be available to fund payment of the Senior Series 2003A Bonds.

The Corporation’s statutory debt issuance capacity under the Act was increased, effective July 15, 2002, to \$1.95 billion through operation of House Bill No. 131 as enacted by the 2002 Regular Session of the General Assembly of the Commonwealth of Kentucky. The Corporation reserves the right: (i) to issue additional Insured Student Loan Revenue Bonds to finance and refinance FFELP Loans; (ii) to enter into financing agreements that are secured on a basis separate and apart from the Senior Series 2003A Bonds and from the Insured Student Loan Revenue Bonds in connection with its Education Finance Program; (iii) to finance education loans that are newly originated or acquired by the Corporation pursuant to any financing arrangement under which funds are available therefor; and (iv) to effect the release of education loans from the lien of any financing arrangement, including the General Bond Resolution, in accordance with the terms thereof through application of amounts available therefor pursuant to any financing arrangement, including the General Bond Resolution.

*Outstanding Student Loan Revenue Bonds.* The following chart sets forth the Outstanding Student Loan Revenue Bonds under the General Bond Resolution:

Series Designation	Original Amount	Amount Outstanding as of March 31, 2002
Senior Series 1997-A-1	\$ 45,250,000	\$ 45,250,000
Senior Series 1997-A-2	45,200,000	45,200,000
Subordinate Series 1997-B	44,550,000	44,550,000
Senior Series 1998A-1	36,400,000	36,400,000
Senior Series 1998A-2	36,400,000	36,400,000
Senior Series 1998B	42,200,000	42,200,000
Senior Series 1999A	51,350,000	51,350,000
Senior Series 1999B	23,650,000	23,650,000
Senior Series 2000A-1	42,100,000	42,100,000
Senior Series 2000A-2	42,100,000	42,100,000
Senior Series 2000A-3	42,050,000	42,050,000
Senior Series 2000B	23,750,000	23,750,000
Senior Series 2001A-1	59,850,000	59,850,000
Senior Series 2001A-2	59,850,000	59,850,000
Subordinate Series 2001B	30,300,000	30,300,000
Senior Series 2002A-1	55,450,000	55,450,000
Senior Series 2002A-2	55,450,000	55,450,000
Senior Series 2002A-3	39,100,000	39,100,000
Total	<u>775,000,000</u>	<u>775,000,000</u>

*Student Loans Securing Student Loan Revenue Bonds.* Following are summaries, as of March 31, 2003 of all Student Loans held under the General Bond Resolution:

<u>Loan Type*</u>	<u>Outstanding Principal</u>	<u>Percent of Total</u>
Stafford and FISL	\$ 527,410,260	78%
PLUS and SLS	19,130,185	3%
Consolidation	130,802,517	19%
Total	<u>\$ 677,342,968</u>	<u>100%</u>

<u>Status*</u>		
Interim (includes loans in school and grace)	\$ 297,846,908	44%
Deferment	72,784,695	11%
Repayment	306,711,365	45%
Total	<u>\$ 677,342,968</u>	<u>100%</u>

<u>School Type*</u>	<u>Outstanding Principal</u>	<u>Percent of Total</u>
Four-Year Public	\$ 314,005,807	57%
Four-Year Private	145,740,541	27%
Two-Year Public and Private	43,798,434	8%
Out-of-State Public and Private	18,640,573	3%
Proprietary	24,355,096	5%
Total	<u>\$ 546,540,451</u>	<u>100%</u>

(Consolidation loans are excluded from the total.)

\* The Corporation has established certain allowances for losses on insured Student Loans that are reflected in its financial statements but not in the preceding summaries.

*Availability of Student Loans.* The Corporation expects to apply all proceeds of the Senior Series 2003A-1 Bonds that are to be initially deposited in the Loan Account, along with all funds made available therefor as a result of the initial application of Senior Series 2003A-2 Bond proceeds, to fund the origination and acquisition of FFELP Loans prior to July 1, 2004. See Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Legislative and Administrative Matters". The General Bond Resolution permits the periodic transfer from the Revenue Account to the Loan Account of Revenues in excess of required Revenue Account applications. See "*Certain Anticipated Transfers Expected to Affect Portfolio Composition*".

The 1993 amendments to the Higher Education Act authorized the implementation of a competing program of direct federal lending. Such implementation may result in an increasing reduction in the volume of FFELP Loans. The federal direct lending program also authorized the Secretary to offer borrowers consolidation loans with income contingent terms if such borrowers are unable to obtain loans with income sensitive repayment terms from any other lender. The number or the dollar volume of FFELP Loans originated, acquired or held by the Corporation or guaranteed by KHEAA may decrease as a result of such implementation and such a decrease may not be proportionate to the percentage by which such implementation reduces the number or the dollar volume of FFELP Loans nationally. Moreover, replacement of FFELP Loans by direct federal lending or some other federal program might affect the availability of FFELP Loans for purchase by the Corporation. While authorization of the Federal Family Education Loan Program and its predecessors has been repeatedly extended, there can be no assurance as to the likelihood of further extension or of any change in present federal policy relative to the financing of post-secondary education. The Corporation does not expect, however, the development of federal policy to have a material adverse effect upon its ability to pay debt service on its Bonds in a timely fashion or to discharge its obligations under the Resolutions. The Corporation further expects that the majority of the Student Loans to be acquired, originated or refinanced through the expenditures of Senior Series 2003A Bond proceeds, or of other amounts becoming available in the Trust Estate, will be Student Loans that have been or will be originated subsequent to July 1, 1994 and that a substantial portion of such Student Loans have been or will be originated subsequent to July 1, 1997. See Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Legislative and Administrative Matters" and "*Federal Direct Student Loan Program*".

*Certain Anticipated Transfers Expected to Affect Portfolio Composition.* The Corporation has determined to adopt a practice of periodically transferring FFELP Loans between trust estates securing Corporation obligations, including the Trust Estate securing the Bonds, for consideration, in order to reduce the overall amount of revenue that the Corporation may receive upon FFELP Loans allocable, for purposes of applicable federal tax regulations, to tax-exempt obligations issued by the Corporation in excess of the maximum amount that may be retained by the Corporation consistent with certain yield limitations imposed by such regulations. It is expected that the first such transfer, to be effected in the current calendar year, will involve a substantial number of Student Loans currently constituting assets of the Trust Estate securing the Bonds and may substantially alter the current composition of the Student Loan portfolio included in the Trust Estate securing the Bonds. The Corporation does not expect any such transfer to: (i) materially adversely affect the adequacy of the Trust Estate to fund the full and timely payment of

debt service and all other payments required under the General Bond Resolution; or (ii) to directly result in the redemption of Bonds. The Resolutions provide that the Corporation may at any time transfer Loans to any trust estate securing Corporation obligations at an aggregate price, in the form of cash or Loans, at least equal to the aggregate principal amount of Loans so transferred (plus accrued interest, interest subsidy payments and special allowance payments thereon).

*Servicing of FFELP Loans and Other Education Loans.* The Corporation currently expects to service all Student Loans held under the Resolutions. It currently services approximately \$812 million outstanding principal amount of FFELP Loans that are pledged pursuant to the Resolutions, the 1997 Resolution or the Line of Credit Trust Agreement and approximately \$3.2 billion of FFELP Loans and other education loans on behalf of other holders, including holders with national lending operations. The majority of such education loans are being serviced by the Corporation pursuant to servicing agreements that do not provide for the acquisition by the Corporation of the education loans serviced. In addition, the Corporation currently collects approximately \$50 million of FFELP Loans and other education loans for other holders on a commission basis. The Corporation expects to enter into additional servicing and collection agreements, and to increase the outstanding balance and number of education loans under existing agreements. The Corporation's servicing obligations pursuant to such servicing and collection agreements are without recourse to assets pledged to secure any Corporation financings, including the Trust Estate established under the Resolutions to secure the Bonds. The Corporation currently subcontracts certain FFELP Loan servicing functions. The Corporation deposits all FFELP Loan payments upon receipt into clearing accounts with financial institutions and periodically transfers payments from such clearing accounts to the applicable holder or fiduciary.

The Corporation currently services its FFELP Loans utilizing software purchased from IFA Systems, a division of Idaho Financial Associates, Inc. ("IFA"), which has been in the student loan business for over 15 years. In January 2002, IFA merged with National Education Loan Network ("Nelnet"), a large national student loan asset manager headquartered in Lincoln, Nebraska. IFA now operates as a subsidiary of Nelnet. The Corporation has entered into an agreement with IFA Systems pursuant to which IFA has agreed to provide, from time-to-time, program changes to assure that the Corporation is able to comply with changes in provisions of the Higher Education Act. IFA Systems also makes certain other software changes and enhancements requested by the Corporation in its role as servicer for various types of loans.

The Higher Education Act requires that the Corporation and its agents and employees exercise "due diligence" in the servicing and collection of FFELP Loans. The Higher Education Act defines "due diligence" to require the holders of a FFELP Loan to utilize collection practices at least as extensive and forceful as those generally practiced by financial institutions for the collection of consumer loans. Federal regulations prescribe a series of actions that must be taken by a lender in the collection of delinquent (past due) FFELP Loans. Additionally, those regulations set forth specific requirements that a lender or holder of FFELP Loans must meet to constitute due diligence in the making, disbursing, and servicing of FFELP Loans. Failure to exercise such reasonable care and diligence may result in the disqualification of an "eligible lender" (which could include the Corporation as a holder of FFELP Loans) from further federal insurance payments on affected loans if the applicable guaranty agency determines that the foregoing standards have not been met. The Corporation or a lender may not relieve itself of its responsibility for meeting these standards by delegation to any servicing agent and, accordingly, if any third party servicer of the Corporation's FFELP Loans fails to meet such standards, the Corporation's ability to realize the benefits of the guaranty agency's insurance payments may be adversely affected.

The Higher Education Act requires that a guaranty agency ensure that due diligence be exercised by lenders in making, servicing and collecting FFELP Loans guaranteed by the guaranty agency. Each guaranty agency must establish procedures and standards for due diligence that are consistent with federal standards. If the Corporation or any third party servicer of the Corporation's FFELP Loans does not comply with the due diligence standards established by the Higher Education Act and federal regulations, then the Corporation's ability to realize the benefits of guarantee payments and the guaranty agency's ability to realize the benefits of federal reinsurance payments may be adversely affected.

The Corporation retains the right to provide for administration of its Education Finance Program in the most economically efficient manner, subject to its contractual obligations in connection with financings. The Corporation has reserved the right to assist student borrowers by reducing up front fees, implementing interest rate

discounts to reward borrowers for a history of timely payments, or other borrower benefits, which may have the effect of reducing loan yield with respect to Student Loans, provided that the Corporation obtains a Rating Affirmation. The Corporation currently pays, on behalf of certain borrowers, varying portions of the up-front fees otherwise payable by such borrowers, equivalent to up to three percent of the principal amount of the borrowers' FFELP Loans. In addition, the Corporation currently discounts interest rates payable by borrowers who have qualified on the basis of making consecutive timely payments, or of agreeing to automatic payment arrangements, by up to two percent. Effective July 1, 2002, borrowers of certain FFELP Loans who make the requisite number of consecutive timely payments will receive a one time credit of 3.5% of the original principal balance of their FFELP Loans instead of the interest rate reduction described in the preceding sentence. The Corporation currently expects to continue to offer these borrower benefits, but reserves the right to discontinue or alter them, and to offer additional or different benefits, in the future.

Prior to an Event of Default, the Trustee has no duties or obligations to service or collect or monitor the servicing and collecting of Student Loans by the Corporation as servicer or any other subservicer. The Trustee also is not be responsible for accounting and reporting functions required under the Higher Education Act to preserve the guarantee of the guarantee agency or the insurance of the Secretary on the Student Loans.

Prior to an Event of Default, the Corporation, and not the Trustee, is the custodian of the Student Loan notes. The Trustee shall have no responsibility for loss of or damage to the Student Loan notes held by the Corporation as the custodian or by its agents. The Corporation as custodian, and not the Trustee, is responsible for reviewing and servicing, respectively, each Student Loan and safekeeping and preserving it. The Trustee shall have no responsibility or liability for examination, safekeeping, preserving, or servicing of the Student Loans.

The Trustee may have certain duties relating to the foregoing matters specified in the preceding two paragraphs upon the occurrence of an Event of Default, as provided in the General Bond Resolution.

## **GUARANTY AGENCIES**

### **General**

The Resolutions permit the application of amounts credited to the Loan Account to finance FFELP Loans that are guaranteed or insured: (i) by KHEAA; (ii) by any other guaranty agency under the Higher Education Act, subject to receipt of a Rating Affirmation; and (iii) by any successor to the obligations of any such entity. The Corporation expects to apply all Senior Series 2003A Bond proceeds to be initially deposited in the Loan Account to finance FFELP Loans that are guaranteed by KHEAA, but reserves the right to apply amounts credited to the Loan Account to finance other education loans in compliance with the Resolutions.

### **The Kentucky Higher Education Assistance Authority**

KHEAA is a public corporation and governmental agency and instrumentality of the Commonwealth established in 1966 to serve the public purpose of improving opportunities for higher education by insuring student loans for students eligible under the Higher Education Act; providing loans, grants, and scholarship awards to qualified Kentucky students; and offering information relating to KHEAA programs to Kentucky residents.

The powers of KHEAA with respect to insuring student loans include: (i) providing loan insurance within the limitations of Kentucky law and the Higher Education Act, the loan in each case to be subject to agreements providing for interest payments, reimbursements, reinsurance and other benefits to the extent provided by the Higher Education Act; (ii) entering into agreements and undertakings with the Secretary to constitute KHEAA as a state agency qualified to insure student loans under the Higher Education Act and to qualify such student loans for interest subsidies, reimbursement, reinsurance, and other benefits available under the Higher Education Act; (iii) entering into contracts with eligible lenders and eligible education institutions to provide for the administration of student financial assistance programs; (iv) collecting from the borrower amounts due under a student loan on which KHEAA has fulfilled its insurance obligations following the inability of the holders to collect such loan; (v) approving, limiting, suspending, or terminating the eligibility of educational institutions or lenders to participate in KHEAA's Loan Guarantee Program, subject to the provisions of the Higher Education Act and applicable Kentucky

law; (vi) if any conflict exists between applicable Commonwealth law and the Higher Education Act that would result in a loss by KHEAA of federal funds, adopting rules, regulations, and policies consistent with the Higher Education Act, but which are not in derogation of the Constitution and general laws of the Commonwealth; (vii) administering federal funds allotted to the Commonwealth in respect of student loans, administrative costs, and other matters; and (viii) receiving funds and acquiring property from any source, public or private, except that KHEAA has no power to make its debts payable out of any funds other than those of KHEAA.

In addition to its student loan guarantee functions, KHEAA offers origination services to lenders, administers two state grant programs, one merit scholarship program, one teacher incentive loan program, one osteopathic medicine scholarship program and the state work-study program to provide financial assistance to eligible students. Such programs are substantially funded by the Commonwealth supplemented by federal funds. Effective May 10, 1990, responsibilities for the Kentucky Education Savings Plan Trust (Trust) were transferred to KHEAA by Executive Order 90-433 ratified by the Kentucky General Assembly. The Trust offers opportunities for families to save for future college costs. Trust funds are fully segregated from all other funds managed by KHEAA.

KHEAA is governed by its Board of Directors, which may officially act by a majority of its voting members. On July 18, 2002, the Governor of the Commonwealth issued an executive order expanding the number of members of the KHEAA's Board of Directors through the addition of eight voting public members of the Corporation's Board of Directors and the President of the Association of Independent Kentucky Colleges and Universities. The executive order has been ratified through operation of Senate Bill No. 17 as enacted by the 2003 Regular Session of the General Assembly of the Commonwealth, and effective June 24, 2003, the composition of KHEAA's Board of Directors is further amended to add as an *ex officio* member the Commissioner of the Kentucky Department of Education. The Board of Directors of KHEAA consists of 19 (20 effective June 24, 2003) members, of whom 15 are appointed by the Governor from the general public residing in the Commonwealth to serve a term of four years each and five serve *ex officio* by reason of their positions as Treasurer of the Commonwealth, President of the Council on Postsecondary Education of the Commonwealth, Secretary of the Finance and Administration Cabinet of the Commonwealth, President of the Association of Independent Colleges and Universities and Commissioner of the Kentucky Department of Education. The Board of Directors elects from its membership a Chair, Chair-elect, and Secretary-Treasurer. The Executive Director of KHEAA is Joe L. McCormick. Dr. McCormick also serves as Executive Director and Chief Executive Officer of the Corporation. KHEAA's office is located at 100 Airport Road, Frankfort, Kentucky 40601, telephone number (502) 696-7200. See "THE CORPORATION—Governance and Functions".

*KHEAA's Loan Guarantee Program.* In November 1978, KHEAA commenced guaranteeing student loans as the state guarantee agency of the Commonwealth under Section 428(c) of the Higher Education Act and in accordance with Kentucky law and KHEAA's agreements with the Secretary.

Pursuant to KHEAA's Loan Guarantee Program, any eligible holder of a loan guaranteed by KHEAA is entitled to reimbursement from KHEAA to the maximum extent permitted by the Higher Education Act for any proven loss incurred resulting from the default, death, permanent and total disability, or discharge in bankruptcy of the borrower and with respect to certain other claims. At the time KHEAA pays a claim for reimbursement of a defaulted loan, the holder must assign to KHEAA all rights accruing to the holder under the note.

On April 18, 1995, an agreement between the Alabama Commission on Higher Education (ACHE) and KHEAA was approved by the U.S. Department of Education for the transition of the Alabama Guaranteed Student Loan Program to KHEAA. KHEAA began to guarantee FFELP Loans for lenders and students in the state of Alabama on June 2, 1995. KHEAA was designated by the U.S. Department of Education as the guarantor for Alabama effective July 1, 1996.

*Loan Insurance Fund.* Pursuant to Kentucky Revised Statutes Sections 164.740 through 164.785, KHEAA has established a Loan Insurance Fund used to account for all loan related activities. The Loan Insurance Fund includes the Federal Student Loan Reserve Fund and an Agency Operating Fund established under the Higher Education Amendments of 1998.

Sources of funds for the Loan Insurance Fund include: (i) insurance premiums for loans guaranteed; (ii) loans processing and issuance and account maintenance fees from the Secretary; (iii) reinsurance from the



Secretary for default and other claims paid; (iv) default collections; (v) and investment income derived from such funds. Uses of funds are default and other claims on loans guaranteed, and operating expenses for loan guarantee functions.

Pursuant to Kentucky Revised Statutes, Sections 164.740 to 164.785, as amended, KHEAA is authorized to issue loan guarantees to eligible lenders on any loans to qualified students, provided that no additional loans may be guaranteed if the total amount of all outstanding student loans guaranteed by KHEAA exceeds seventy-five times the funds available in the Loan Insurance Fund. Funds available in the Loan Insurance Fund are calculated on the basis of the net assets before deducting unearned insurance premiums, which equals the fund balance plus unearned insurance premiums. Funds available in the Loan Insurance Fund are restricted by federal regulations and the Higher Education Act.

Outstanding loan guarantee commitments by ACHE, on which no claims had been filed or paid, were assumed by KHEAA on December 31, 1995. Accounts held by ACHE on which default claims were paid prior to April 13, 1993, that remained in active repayment status and accounts held by ACHE on which default claims were paid after April 15, 1993, were transferred to KHEAA prior to June 30, 1996. Following the transfer of defaulted accounts, remaining Alabama federal reserve funds were transferred to KHEAA and credited to the Loan Insurance Fund.

Pursuant to the 1997 Amendments, KHEAA paid approximately \$14 million (its proportionate share of guarantee agency reserves to be paid for federal deficit reduction) to the Secretary on September 1, 2002. The 1998 Amendments also require smaller proportionate reserve returns in 2002, 2006 and 2007. On July 11, 2002, the Secretary notified KHEAA that its share of the reserve returns in 2002, 2006 and 2007 would be approximately \$3.5 million. KHEAA paid \$1 million towards its share of the reserve returns on September 1, 2002. See Appendix A, "SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM—Federal Insurance and Reinsurance and Reimbursement of Guaranty Agencies".

The following table summarizes the student loans guaranteed by KHEAA (and reinsured by the Secretary) annually, the aggregate outstanding guarantee commitment for the periods indicated, and KHEAA's Claims Rate for purposes of reinsurance. The Coverage Ratio set forth below is determined by dividing the funds available in the Loan Insurance Fund by the principal amount of the aggregate outstanding guarantee commitment.

Fiscal Year Ended <u>June 30</u>	Annual Principal Amount of <u>Loans Guaranteed</u>	Aggregate Principal Guarantee <u>Commitment</u>	Coverage <u>Ratio</u>	Claims <u>Rate*</u>
1997	314,023,470	1,625,863,960	2.60	4.22
1998	330,006,170	1,637,204,817	2.35	3.88
1999	345,249,100	1,779,865,400	1.95	2.78
2000	454,779,609	1,976,730,128	1.48	1.43
2001	542,872,356	1,947,932,104	1.35	1.62
2002	662,753,138	2,336,677,000	0.84	1.73

\*At federal fiscal year ending September 30.

*No Pledge of KHEAA's Funds and Assets.* The funds and assets of KHEAA are not pledged to or available for payment of the Bonds. Funding of KHEAA's operations is subject to authorization by the General Assembly of the Commonwealth.

## CONTINUING DISCLOSURE

### General

In accordance with the requirements of Rule 15c2-12 (the “Rule”) promulgated by the Securities and Exchange Commission (the “SEC”), the Corporation will enter into a continuing disclosure undertaking (the “Continuing Disclosure Agreement”) with the Trustee for the Senior Series 2003A Bonds, which shall constitute a written undertaking for the benefit of the respective owners of such Bonds, solely to assist the underwriter in complying with subsection (b)(5) of the Rule.

The Corporation will agree in the Continuing Disclosure Agreement to provide to the Trustee, which shall provide within 5 Business Days after receipt thereof, to each nationally recognized municipal securities information repository and any public or private repository or entity designated by the State as a state repository for purposes of subsection (b)(5) of the Rule (each, a “Repository”), annual financial information and operating data (the “Annual Financial Information”) relating to it and any Additional Obligated Persons (defined below) covering the matters described under “Annual Financial Information” below. The Corporation will also agree to provide to each Repository, in a timely manner, notice of any of the events (“Event Notice”) if determined by the Corporation to be material, as described under “Event Notices” below.

The Corporation has never failed to comply in all material respects with any previous undertakings with regard to said Rule to provide Annual Financial Information or notices of material events. The on-going disclosure obligations of the Corporation shall terminate upon the full payment, prior redemption or legal defeasance of the Senior Series 2003A Bonds, or with respect to any Additional Obligated Person, at the time that the party no longer meets the definition of Additional Obligated Person.

The Corporation may appoint or engage a dissemination agent to assist in carrying out its obligations under the Continuing Disclosure Agreement.

The Corporation may amend the Continuing Disclosure Agreement, and waive any provision thereof, by written agreement of the parties, without the consent of the respective owners of the Senior Series 2003A Bonds (except to the extent required under clause (4)(ii) below) if all of the following conditions are satisfied: (1) such amendment is made in connection with a change in circumstances that arises from a change in legal (including regulatory) requirements, a change in law (including rules or regulations) or in interpretations thereof, or a change in the identity, nature or status of the Corporation or any Additional Obligated Person or the type of business conducted thereby; (2) the Continuing Disclosure Agreement as so amended would have complied with the requirements of the Rule as of the date of the Continuing Disclosure Agreement, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; (3) the Corporation shall have delivered to the Trustee an opinion of nationally recognized bond counsel or counsel expert in federal securities laws, addressed to the Corporation and the Trustee, to the same effect as set forth in clause (2) above; (4) either (i) the Corporation shall have delivered to the Trustee an opinion of nationally recognized bond counsel or counsel expert in federal securities laws, addressed to the Corporation and the Trustee, to the effect that the amendment does not materially impair the interests of the holders of the Senior Series 2003A Bonds, or (ii) the holders of the Senior Series 2003A Bonds consent to the amendment to the Continuing Disclosure Agreement pursuant to the same procedures as are required for amendments to the Resolutions with consent of holders of the Senior Series 2003A Bonds pursuant to the terms of the Resolutions as in effect on the date of the Continuing Disclosure Agreement; and (5) the Corporation shall have delivered copies of such opinion and amendment to each Repository.

In the event of default by the Corporation of its obligations under the Continuing Disclosure Agreement to provide continuing disclosure, the Beneficial Owners of the Senior Series 2003A Bonds and the Trustee on behalf of such owners may take action to compel compliance, provided that any enforcement action by any such person shall be limited to a right to obtain specific enforcement of the Corporation’s obligations under the Continuing Disclosure Agreement. No such default under the Continuing Disclosure Agreement shall constitute an Event of Default under the Resolutions.

## **Annual Financial Information**

The Corporation will provide Annual Financial Information for the Corporation and any Additional Obligated Person within 270 days of the end of such party's fiscal year (the "Reporting Date"), beginning with the fiscal year in each case ending on or after July 1, 2003. Such Annual Financial Information shall consist of the following information:

(I) Annual audited financial statements for the Corporation and for any Additional Obligated Person prepared in accordance with generally accepted accounting principles.

(II) An update of the tabular information presented under the heading "THE CORPORATION" or the heading "GUARANTY AGENCIES" in this Official Statement.

If the audited financial statements for the Corporation or the Additional Obligated Person, as the case may be, are not available by the Reporting Date, unaudited financial statements of the Corporation or an Additional Obligated Person, as the case may be, are to be provided as part of the applicable Annual Financial Information and audited financial statements for the Corporation or an Additional Obligated Person, as the case may be, when and if available, will be provided to the Trustee and each Repository. If the fiscal year of the Corporation or an Additional Obligated Person, as the case may be, changes, the Corporation or an Additional Obligated Person, as the case may be, shall give notice of such change in the same manner and time as an Event Notice.

## **Event Notice**

In addition to the Annual Financial Information described above, the Corporation will also agree to provide an Event Notice upon the happening of and with respect to any of the following events, if material, with respect to the applicable Series of Senior Series 2003A Bonds:

- (1) Principal and interest payment delinquencies;
- (2) Nonpayment related defaults;
- (3) Unscheduled draws on the debt service reserves reflecting financial difficulties;
- (4) Unscheduled draws on credit enhancements reflecting financial difficulties;
- (5) Substitution of credit or liquidity providers, or their failure to perform;
- (6) Adverse tax opinions or events adversely affecting the tax exempt status of the Senior Series 2003A Bonds;
- (7) Modifications to rights of owners of the applicable Series of Senior Series 2003A Bonds;
- (8) Calls of the applicable Series of Senior Series 2003A Bonds;
- (9) Defeasances of the applicable Series of Senior Series 2003A Bonds;
- (10) Release, substitution or sale of assets securing repayment of the applicable Series of Senior Series 2003A Bonds; and
- (11) Rating changes.

## **Definitions**

"Additional Obligated Person" means, prior to receipt by the Trustee of a Negative Opinion or the issuance of a written interpretation by the Staff of the SEC, any Guarantor that is guaranteeing student loans having an aggregate principal amount of at least 20% of the aggregate principal amount of all student loans.

"Negative Opinion" means an opinion with respect to a person or entity that is issued by a nationally recognized bond counsel firm or counsel expert in federal securities laws, which counsel and opinion are in form and substance acceptable to the Corporation, to the effect that such person or entity does not constitute an "obligated person" with respect to the Senior Series 2003A Bonds within the meaning of the Rule.

## Repository

A listing of active NRMSIR's and contact information for each such NRMSIR is currently made available by the SEC on its website at <<http://www.sec.gov/info/municipal/nrmsir.htm>>. The following are the current repositories for the purposes of the continuing disclosure required under each Continuing Disclosure Agreement:

Bloomberg Municipal Repository  
100 Business Park Drive  
Skillman, NJ 08558  
E-Mail Address: Munis@Bloomberg.com  
Telephone: (609) 279-3225  
Fax: (609) 279-5962

DPC Data Inc.  
One Executive Drive  
Fort Lee, NJ 07024  
E-Mail Address: nrmsir@dpcdata.com  
Telephone: (201) 346-0701  
Fax: (201) 947-0107

Standard & Poor's J.J. Kenny Repository  
55 Water Street  
45<sup>th</sup> Floor  
New York, New York 10041  
E-Mail Address: nrmsir\_repository@sandp.com  
Telephone: (212) 438-4595  
Fax: (212) 438-3975

FT Interactive Data  
Attn: NRMSIR  
100 William Street  
New York, New York 10038  
E-Mail Address: NRMSIR@FTID.com  
Telephone: (212) 771-6999  
Fax: (212) 771-7390 (Secondary Market Information)  
(212) 771-7391 (Primary Market Information)

## TAX MATTERS

### Opinion of Bond Counsel

In the opinion of Hawkins, Delafield & Wood, Bond Counsel, under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein, (i) interest on the Senior Series 2003A Bonds is excluded from gross income for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and (ii) interest on the Senior Series 2003A Bonds, however, is treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code. In rendering its opinion, Bond Counsel has relied on certain representations, certifications of fact, and statements of reasonable expectations made by the Corporation in connection with the Senior Series 2003A Bonds, and Bond Counsel has assumed compliance by the Corporation with certain ongoing covenants to comply with applicable requirements of the Code to assure the exclusion of interest on the Senior Series 2003A Bonds from gross income under Section 103 of the Code.

In addition, in the opinion of Bond Counsel, under existing statutes, the Senior Series 2003A Bonds, the income thereon, and the transfer thereof, including any profit made on the sale thereof, shall at all times be exempt from taxation or assessment of any type by the Commonwealth, its agencies and departments and by all political subdivisions within the Commonwealth.

Bond Counsel expresses no opinion regarding any other federal or state tax consequences with respect to the Senior Series 2003A Bonds. Bond Counsel renders its opinion under existing statutes and court decisions as of the Issue Date, and assumes no obligation to update its opinion after the Issue Date to reflect any future action, fact or circumstance, or change in law or interpretation, or otherwise. Bond Counsel expresses no opinion on the effect of any action hereafter taken or not taken in reliance upon an opinion of other counsel on the exclusion from gross income for federal income tax purposes of interest on the Senior Series 2003A Bonds, or under state and local tax law.

### Certain Ongoing Federal Tax Requirements and Covenants

The Code establishes certain ongoing requirements that must be met subsequent to the issuance and delivery of the Senior Series 2003A Bonds in order that interest on the Senior Series 2003A Bonds be and remain excluded from gross income under Section 103 of the Code. These requirements include, but are not limited to,

requirements relating to use and expenditure of gross proceeds of the Senior Series 2003A Bonds, yield and other restrictions on investments of gross proceeds, and the arbitrage rebate requirement that certain excess earnings on gross proceeds be rebated to the federal government. Noncompliance with such requirements may cause interest on the Senior Series 2003A Bonds to become included in gross income for federal income tax purposes retroactive to their Issue Date, irrespective of the date on which such noncompliance occurs or is discovered. The Corporation has covenanted to comply with certain applicable requirements of the Code to assure the exclusion of interest on the Senior Series 2003A Bonds from gross income under Section 103 of the Code.

### **Certain Collateral Federal Tax Consequences**

The following is a brief discussion of certain collateral federal income tax matters with respect to the Senior Series 2003A Bonds. It does not purport to address all aspects of federal taxation that may be relevant to a particular owner of a Senior Series 2003A Bond. Prospective investors, particularly those who may be subject to special rules, are advised to consult their own tax advisors regarding the federal tax consequences of owning and disposing of the Senior Series 2003A Bonds.

Prospective owners of the Senior Series 2003A Bonds should be aware that the ownership of such obligations may result in collateral federal income tax consequences to various categories of persons, such as corporations (including S corporations and foreign corporations), financial institutions, property and casualty and life insurance companies, individual recipients of Social Security and railroad retirement benefits, individuals otherwise eligible for the earned income tax credit, and taxpayers deemed to have incurred or continued indebtedness to purchase or carry obligations the interest on which is not included in gross income for federal income tax purposes. Interest on the Senior Series 2003A Bonds may be taken into account in determining the tax liability of foreign corporations subject to the branch profits tax imposed by Section 884 of the Code.

### **Legislation**

Legislation affecting municipal bonds is regularly under consideration by the United States Congress. There can be no assurance that legislation enacted or proposed after the date of issuance of the Senior Series 2003A Bonds will not have an adverse effect on the tax-exempt status or market price of the Senior Series 2003A Bonds.

## **LEGALITY FOR INVESTMENT**

Subject to any applicable federal requirements or limitations, the Senior Series 2003A Bonds in the Commonwealth are securities in which all public officers and public bodies of the Commonwealth, political subdivisions thereof, insurance companies, trust companies, banking associations, investment companies, executors, administrators, trustees, and other fiduciaries may properly and legally invest funds, including capital, in their control or belonging to them.

## **ABSENCE OF MATERIAL LITIGATION**

There is no controversy or litigation of any nature pending or threatened to restrain or enjoin issuance, sale, execution or delivery of the Senior Series 2003A Bonds, or in any way contesting or affecting the validity of the Senior Series 2003A Bonds, any proceedings of the Corporation taken with respect to the issuance of sale thereof; and as of the date hereof, there is no litigation pending, or threatened that would materially adversely affect the pledge or application of any moneys or security provided for the payment of the Senior Series 2003A Bonds or the powers of the Corporation.

## **APPROVAL OF LEGALITY**

Certain legal matters in connection with the Senior Series 2003A Bonds are to be passed upon by Hawkins, Delafield & Wood, New York, New York, Bond Counsel. Certain legal matters are to be passed upon for the Underwriter by its counsel, Squire, Sanders & Dempsey L.L.P. The unqualified approving opinion of Bond Counsel to the Corporation shall accompany each of the Senior Series 2003A-1 Bonds and the Senior Series 2003A-2 Bonds substantially in the respective form attached to this Official Statement as Appendix E.

## **RATINGS**

Moody's is expected to assign its municipal bond rating of "Aaa" to the Senior Series 2003A Bonds. Standard and Poor's is expected to assign its municipal bond rating of "AAA" to the Senior Series 2003A Bonds. Such ratings reflect only the view of the respective Rating Agency and an explanation of the significance of such ratings can only be obtained from the respective Rating Agency. There is no assurance that such ratings will be continued for any given period of time or that they will not be revised downward or withdrawn entirely if, in the judgment of the respective Rating Agency, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect upon the market price or the marketability of the Senior Series 2003A Bonds.

## **UNDERWRITING**

The Senior Series 2003A Bonds will be purchased by the Underwriter at a purchase price equal to the aggregate face amount of the Senior Series 2003A Bonds plus accrued interest, if any. The Corporation has agreed to pay the Underwriter an underwriting fee equal to \$208,319.

## **APPROVAL OF ISSUANCE OF THE SENIOR SERIES 2003A BONDS**

Issuance of the Senior Series 2003A Bonds by the Corporation was approved by the Governor of the Commonwealth. The Corporation expects the issuance of the Senior Series 2003A Bonds to receive all necessary state approvals.

## **INDEPENDENT ACCOUNTANTS**

The Corporation's financial statements as of June 30, 2002 and 2001 and for the years then ended, included in this Official Statement, have been audited by PricewaterhouseCoopers LLP, independent accountants, as stated in their report appearing in Appendix D hereto. See "MISCELLANEOUS".

## **MISCELLANEOUS**

*Since the Senior Series 2003A Bonds are special and limited obligations of the Corporation, payable solely from the Trust Estate pledged under the Resolutions, the overall financial status of the Corporation does not indicate and does not necessarily affect whether such revenues and other amounts will be available under the Resolutions to pay the principal of and interest on the Senior Series 2003A Bonds. The Corporation is not obligated to pay any amounts in respect of principal and/or interest on the Senior Series 2003A Bonds from any moneys legally available to the Corporation for its general purposes other than those expressly pledged.*

The information set forth in this Official Statement relating to the Corporation and KHEAA was obtained from the records of the Corporation and KHEAA and from other sources considered reliable.

All quotations from, and summaries and explanations of, the Higher Education Act, the Act, the State Guarantee Act and the Resolutions contained herein do not purport to be complete and reference is made to such

laws and documents for full and complete statements of their provisions. The Appendices attached hereto are part of this Official Statement. Copies of the Act and the Resolutions may be obtained upon written request directed to the Corporation, P.O. Box 24266, Louisville, Kentucky 40224-0266.

Any statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact.

This Official Statement is not to be construed as a contract or agreement between the Corporation and the purchasers or owners of any Bonds.

**KENTUCKY HIGHER EDUCATION  
STUDENT LOAN CORPORATION**

By: /s/ Dr. Joe L. McCormick  
Executive Director and Chief Executive Officer

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## **Appendix A**

### **Summary of Certain Provisions of the Federal Family Education Loan Program**

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## SUMMARY OF CERTAIN PROVISIONS OF THE FEDERAL FAMILY EDUCATION LOAN PROGRAM

Title IV of the Higher Education Act provides for a program (the “Federal Family Education Loan Program,” the “FFEL Program”) pursuant to which Loans are made (collectively, “FFELP Loans”) to students and parents of dependent students, which loans are: (i) guaranteed by a state agency or private non-profit corporation and reinsured by the federal government; or (ii) directly insured by the federal government. Several types of FFELP Loans are currently authorized under the FFEL Program: (i) fully subsidized loans to students who demonstrate need on the basis of certain tests, currently known as Federal Stafford Loans (“Subsidized Stafford Loans”); (ii) generally similar loans, with respect to the full amount borrowed to students who do not pass such need tests, currently known as Federal Unsubsidized Stafford Loans (“Unsubsidized Stafford Loans” and, collectively with Subsidized Stafford Loans, “Stafford Loans”); (iii) loans to parents of students who are dependents, currently known as Federal PLUS Loans (“PLUS Loans”); and (iv) loans to consolidate the borrower’s obligations under various federally authorized student loan programs into a single loan, currently known as Federal Consolidation Loans (“FFEL Consolidation Loans”). Prior to July 1, 1994, the FFEL Program also included a separate type of loan to graduate and professional students and, under certain circumstances, undergraduate students, to supplement their Stafford Loans (“Supplemental Loans to Students” or “SLS Loans”). The principal federal benefits that the FFEL Program provides to holders of loans originated thereunder are: (i) federal interest subsidy payments to holders of certain loans in lieu of borrower payments during certain periods defined by borrower status (“Interest Subsidy Payments”); (ii) federal special allowance payments to holders of certain loans during certain periods defined by interest rate levels (“Special Allowance Payments”); and (iii) federal insurance by the federal Department of Education (the “Department”) or federal reinsurance by the Department of guarantees provided by guaranty agencies. See “—Interest Subsidy Payments on Subsidized Stafford Loans,” “—Special Allowance Payments,” and “—Federal Insurance and Reinsurance and Reimbursement of Guaranty Agencies”.

This summary of the FFEL Program and the Federal Direct Student Loan Program as established by the Higher Education Act describes certain elements of such programs as of the date of this Official Statement and does not purport to be comprehensive or definitive and is qualified in its entirety by reference to the Higher Education Act and the regulations thereunder.

### Legislative and Administrative Matters

Title IV of the Higher Education Act is subject to periodic legislative reauthorization, which was most recently accomplished through operation of the Higher Education Amendments of 1998 (the “1998 Amendments”). Both Title IV of the Higher Education Act and the regulations promulgated thereunder have been the subject of frequent and extensive amendments in recent years and there can be no assurance that further amendment will not materially change the provisions described herein or the effect thereof. In addition, the operation of the FFEL Program has recently been, and may be, affected by proposed and enacted federal budgetary and tax legislation. Recent legislation substantially affecting the FFEL Program includes: (i) the Omnibus Budget Reconciliation Act of 1990 (the “1990 Budget Act”); (ii) the Higher Education Amendments of 1992 (the “1992 Amendments”); (iii) the Student Loan Reform Act of 1993 (the “1993 Amendments”); (iv) the Higher Education Technical Amendments Act of 1993 (the “1993 Technical Amendments”); (v) the Balanced Budget Act of 1997; (vi) the Emergency Student Loan Consolidation Act of 1997; (vii) the Intermodal Surface Transportation Efficiency Act of 1998 (the “1998 Transportation Act”); (viii) the 1998 Amendments; (ix) the Ticket to Work and Work Incentives Improvement Act of 1999 (the “1999 Amendments”); (x) the Higher Education Relief Opportunities for Students Act of 2001; (xi) the 2002 Amendments to the Higher Education Act (the “2002 Amendments”); and (xii) the Bob Stump National Defense Authorization Act for Fiscal Year 2003.

Origination of FFELP Loans is authorized only for limited periods of time. For example, initial disbursement of FFELP Loans to new borrowers pursuant to the FFEL Program is currently authorized to September 30, 2004 (or, in the case of borrowers who have received loans prior to that date, to September 30, 2008, except that authority to make Consolidation Loans under the FFEL Program expires on September 30, 2004). See “—*Certain Recent Developments*” below.

*Certain Recent Developments.* The Corporation currently expects that a majority of the FFELP Loans that may be added to the Trust Estate through the expenditure of Senior Series 2003 Bond proceeds, or of other amounts becoming available in the Trust Estate, will be FFELP Loans which have been or will be originated subsequent to July 1, 1994, and that a substantial portion of such FFELP Loans have been or will be originated subsequent to July 1, 1997. In addition, although the Resolution permits the acquisition of FFELP Loans without regard to date of origination, the Corporation does not currently expect that a material portion of FFELP Loans originated prior to October 1, 1992, or to borrowers with outstanding FFELP Loans originated on or prior to such date, will be included in the Trust Estate. The interest rates and formula for determining Special Allowance Payments applicable to FFELP Loans prior to July 1, 1998 are not specifically described in the following sections of this summary. See “THE CORPORATION – Certain Anticipated Transfers Expected to Affect Portfolio Composition.”

The 1998 Transportation Act changed the interest rate and Special Allowance Payment formulas for Stafford Loans and PLUS Loans disbursed during the period from July 1, 1998 through September 30, 1998. Stafford Loans originated during this period bear interest, during in-school grace and deferment periods, at the average bond equivalent rate of 91-Day Treasury bills (the “91-Day T-Bill Rate”) plus 1.7 percent, with a maximum rate of 8.25 percent, and otherwise bear interest at a rate equivalent to the 91-Day T-Bill Rate plus 2.3 percent, with a maximum rate of 8.25 percent. PLUS Loans disbursed during this period bear interest at a rate equivalent to the 91-Day T-Bill Rate plus 3.1 percent, with a maximum rate of 9 percent. In addition, holders of Stafford Loans are entitled to receive Special Allowance Payments, during in-school and grace periods, based upon the 91-Day T-Bill Rate plus 2.2 percent and, otherwise, based upon the 91-Day T-Bill Rate plus 2.8 percent. Holders of PLUS Loans are entitled to receive Special Allowance Payments, when the 9 percent maximum rate applies, based upon the 91-Day T-Bill Rate plus 3.1 percent. See “– Special Allowance Payments” below.

Under the 1998 Amendments, Stafford Loans disbursed during the period from October 1, 1998 through June 30, 2003 bear interest, during in-school, grace and deferment periods, at a rate equivalent to the 91-Day T-Bill Rate plus 1.7 percent, with a maximum rate of 8.25 percent, and otherwise bear interest at a rate equivalent to the 91-Day T-Bill Rate plus 2.3 percent, with a maximum rate of 8.25 percent. PLUS Loans disbursed during this period bear interest at a rate equivalent to the 91-Day T-Bill Rate plus 3.1 percent, with a maximum rate of 9 percent. FFEL Consolidation Loans disbursed during this period bear interest at a rate equal to the weighted average of the loans consolidated, rounded to the nearest higher one-eighth of 1 percent, with a maximum rate of 8.25 percent. In addition, holders of Stafford Loans disbursed during the period from October 1, 1998 through June 30, 2003 are entitled to receive Special Allowance Payments, during in-school and grace periods, based upon the 91-Day T-Bill Rate plus 2.2 percent and, otherwise, based upon the 91-Day T-Bill Rate plus 2.8 percent. Holders of PLUS and FFEL Consolidation Loans disbursed during this period are entitled to receive Special Allowance Payments, when the applicable maximum rates apply, based upon the 91-Day T-Bill Rate plus 3.1 percent.

Under the 1999 Amendments: (i) holders of Stafford Loans disbursed during the period from January 1, 2000 through June 30, 2003 are entitled to receive Special Allowance Payments, during in-school, grace and deferment periods, based upon the average of the bond equivalent rates of the 3-month commercial paper (Financial) rate as reported by the Federal Reserve (the “CP Rate”) plus 1.74 percent and, otherwise, based upon the CP Rate plus 2.34 percent; and (ii) holders of PLUS and FFEL Consolidation Loans disbursed during this period are entitled, when maximum rates apply, to receive Special Allowance Payments based upon the CP Rate plus 2.64 percent.

Under the 2002 Amendments, the interest rate formulas have been extended with respect to Stafford Loans and PLUS Loans to loans disbursed by June 30, 2006, and with respect to FFEL Consolidation Loans for which an application is received by an eligible lender by June 30, 2006. Interest rates for FFELP Loans pursuant to the 2002 Amendments would be: (i) a fixed rate of 6.8 percent with respect to Stafford Loans disbursed on or after July 1, 2006; (ii) a fixed rate of 7.9 percent with respect to PLUS Loans disbursed on or after July 1, 2006; and (iii) a rate equal to the lesser of (A) the weighted average of the interest rates on the loans consolidated rounded up to the nearest higher one eighth of one percent, or (B) 8.25 percent, with respect to FFEL Consolidation Loans for which an application is received by an eligible lender on or after July 1, 2006. The 2002 Amendments also provide for the extension of the formula for determining special allowance payments to eligible lenders for FFELP Loans disbursed by June 30, 2006, or disbursed on or after July 1, 2006, but only with respect to in-school, grace or deferment periods. See “Special Allowance Payments” below.

Congress has adopted and is considering additional legislation that provides for, among other things, interest rate caps and additional periods of deferment with respect to Insured Student Loans made to the members of the military, including reservists.

### **Eligible Borrowers and Institutions**

FFELP Loans may only be made to Qualified Students and parents of dependent Qualified Students or to consolidate obligations under various federally authorized student loan programs. A “Qualified Student” is generally defined as a citizen, national or permanent resident of the United States or otherwise eligible individual under federal regulations who: (i) has been accepted for enrollment or is enrolled and is maintaining satisfactory progress in a program leading to a recognized educational credential at an eligible institution; (ii) is carrying at least one-half of the normal full-time academic workload for the course of study the student is pursuing, as determined by such institution; (iii) has agreed to notify promptly the holder of the FFELP Loan of any address change or certain changes in status; (iv) meets the “need” requirements, if applicable, for the particular FFEL Program; (v) if he or she is an undergraduate student enrolled in an institution participating in the Pell Grant Program, has had his or her eligibility or ineligibility for the Pell Grant Program has been determined; and (vi) does not owe a refund on grants and is not in default on any Higher Education Act Loan except as specifically permitted by the Higher Education Act. FFELP Loans are unsecured loans, which may be documented, and in which a security interest may be perfected, as provided in the Higher Education Act.

Eligible institutions include institutions of higher education, postsecondary vocational institutions, proprietary institutions of higher education, and institutions outside of the United States which are approved by the Secretary. Eligible institutions of higher education must meet certain standards, which generally provide that the institution: (i) only admits persons who have a high school diploma or its equivalent, or persons who are beyond the age of compulsory school attendance; (ii) is legally authorized to provide a program of postsecondary education within a State; (iii) provides a program for which it awards a bachelor’s degree, a program of not less than two years acceptable for full credit toward a bachelor’s degree or a program of not less than one year to prepare students for gainful employment in a recognized occupation; (iv) is a public or non-profit institution; and (v) is accredited by a nationally recognized accrediting agency or is determined by the Secretary to be likely to meet the standards of an accredited institution. Eligible postsecondary vocational institutions include educational institutions that provide an eligible program of training to prepare students for gainful employment in a recognized occupation, that otherwise comply with the standards applicable to institutions of higher education and that have been in existence for at least two years. Eligible proprietary institutions of higher education include schools, other than public or non-profit institutions, that provide an eligible program of training to prepare students for gainful employment in a recognized occupation, that otherwise comply with the standards applicable to institutions of higher education, that have been in existence for at least two years and which receive at least 10 percent of revenues from sources other than specified federal programs, including the FFEL Program. With certain exceptions, an institution with a cohort default rate that is higher over a period of time than the specified thresholds in the Higher Education Act is not an eligible institution. An institution’s cohort default rate is generally based on the percentage of its current and former students who default on their Stafford Loans or SLS Loans within a specified period of time after entering repayment. The general threshold for such disqualification is currently 25 percent.

With specified exceptions, institutions are excluded from consideration as eligible institutions if the institution: (i) offers more than 50 percent of its courses by correspondence; (ii) enrolls 50 percent or more of its students in correspondence courses; (iii) has a student enrollment in which more than 25 percent of the students are incarcerated; or (iv) has a student enrollment in which more than 50 percent of the students are admitted without a high school diploma or its equivalent and does not provide a two or four year program of instruction. Further, institutions are specifically excluded from participation if: (i) the institution has filed for bankruptcy; or (ii) the owner, or its chief executive officer, has been convicted or pled *nolo contendere* or guilty to a crime involving the acquisition, use or expenditure of federal student aid funds, or has been judicially determined to have committed fraud involving funds under the student aid program. In order to participate in the FFEL Program, the eligibility of an institution must be approved by the Department under standards established by regulation.

## Financial Need Analysis

FFELP Loans may generally be made in amounts, subject to certain limits and conditions, to cover the student's estimated costs of attendance, including tuition and fees, books, supplies, room and board, transportation and miscellaneous personal expenses (as determined by the institution). Each Stafford Loan borrower must undergo a need analysis, which requires the borrower to submit a need analysis form to a multiple data entry processor, which then forwards the information to a federal central processor. The central processor evaluates the parents' and student's financial condition under federal guidelines and calculates the amount that the student and/or the family must contribute towards the student's cost of education (the "Family Contribution"). After receiving information on the family contribution, the institution then subtracts the Family Contribution from its costs of attendance to determine the student's eligibility for grants, loans, and work assistance. The difference between the amount of grants and Subsidized Stafford Loans for which the borrower is eligible and the student's estimated costs of attendance (the "Unmet Need") may be borrowed through Unsubsidized Stafford Loans, subject to certain loan limits. Parents may finance the Family Contribution amount through their own resources or through PLUS Loans. Provisions addressing the implementation of need analysis and the relationship between Unmet Need for financing and the availability of Subsidized Stafford Loan funding have been the subject of frequent and extensive amendments in recent years. There can be no assurance that further amendment to such provisions will not materially affect the availability of Subsidized Stafford Loan funding to borrowers or the availability of Subsidized Stafford Loans for secondary market acquisition.

## Stafford Loans Generally

*Interest.* Stafford Loans bear interest at a rate not in excess of 7 percent per annum if made to a borrower to cover costs of instruction for any period beginning prior to January 1, 1981, or if a subsequent Stafford Loan is made to such a borrower. Stafford Loans made to new borrowers for periods of instruction beginning during the period from January 1, 1981 through September 12, 1983, and subsequent Stafford Loans to such borrowers, bear interest at a rate of 9 percent per annum. Stafford Loans made to new borrowers for periods of enrollment beginning during the period from September 13, 1983 through June 30, 1988 and subsequent Stafford Loans to such borrowers, bear interest at a rate of 8 percent per annum. Stafford Loans made to new borrowers for periods of enrollment beginning during the period from July 1, 1988 through September 30, 1992 pursuant to Section 427A of the Higher Education Act ("427A Loans") initially bore interest at rates of 8 percent per annum from disbursement through four years after repayment commences and 10 percent per annum thereafter, subject to a provision requiring periodic discharge of principal, or payment to the Secretary, to the extent that quarterly interest so calculated exceeded the amount that would result from application of the 91-Day T-Bill Rate for such quarter, plus 3.25 percent, or, with respect to 427A Loans disbursed to new borrowers during the period from July 24, 1992 through September 30, 1992, plus 3.1 percent. However, all 427A Loans were required, under the 1993 Technical Amendments, to be converted by January 1, 1995 to variable rate loans bearing interest at the 91-Day T-Bill Rate plus 3.25 percent or, with respect to 427A Loans disbursed to new borrowers during the period from July 24, 1992 through September 30, 1992, plus 3.1 percent. Stafford Loans first disbursed to new borrowers during the period from October 1, 1992 through June 30, 1994, and subsequent Stafford Loans to such borrowers, bear interest at the 91-Day T-Bill Rate plus 3.1 percent, not to exceed 9 percent. Stafford Loans first disbursed during the period from July 1, 1994 through June 30, 1998, for periods of enrollment beginning on or after the earlier such date, bear interest, subject to the next succeeding sentence, at the 91-Day T-Bill Rate plus 3.1 percent, not to exceed 8.25 percent. Stafford Loans first disbursed during the period from July 1, 1995 through June 30, 1998, for periods of enrollment beginning on or after the earlier such date, during in-school, grace and deferment periods, bear interest at the 91-Day T-Bill Rate plus 2.5 percent, not to exceed 8.25 percent. Stafford Loans first disbursed during the period from July 1, 1998 through June 30, 2006 bear interest, during the in-school, grace and deferment periods, at the 91-Day T-Bill Rate plus 1.7 percent, and otherwise at the 91-Day T-Bill Rate plus 2.3 percent, not to exceed 8.25 percent. See "—Legislative and Administrative Matters — *Certain Recent Developments*" above.

*Loan Limits.* From January 1, 1987 through September 30, 1993, undergraduates were able to borrow up to \$2,625 annually through the completion of the second year of instruction and, prior to July 1, 1993, \$4,000 annually through the remainder of undergraduate study pursuant to Stafford Loans. Stafford Loans for which the first disbursement was made prior to July 1, 1993 are subject to an aggregate limit of \$17,250 for undergraduate study, while graduate or professional students, who may borrow up to \$7,500 annually, are subject to an aggregate limit of \$54,750, inclusive of loans for undergraduate study. The annual loan limit for undergraduate loans first disbursed

on or after July 1, 1993 is dependent on the class year of the borrower and the length of the academic year, and ranges from a minimum annual limit of \$2,625 for first year undergraduate borrowers to a maximum annual limit of \$5,500 for undergraduate borrowers who have successfully completed their first and second years of undergraduate study. The annual loan limit for graduate and professional loans for periods of enrollment beginning on or after October 1, 1993 is \$8,500. Loans for which the first disbursement is made on or after July 1, 1993, are subject to an aggregate limit of \$23,000 for undergraduate students and an aggregate limit of \$65,500 for graduate or professional students, excluding PLUS Loans and SLS Loans. Notwithstanding the foregoing limits, however, additional Unsubsidized Stafford Loans are currently available to independent, and to certain dependent, undergraduate students, in annual amounts up to \$5,000, and to graduate and professional students, in annual amounts up to \$10,000, subject to overall limits on any borrower's aggregate outstanding Stafford Loans, Unsubsidized Stafford Loans, analogous loans made under the Federal Direct Student Loan Program and SLS Loans of \$46,000, for undergraduate students, and of \$138,500, for graduate or professional students. Under the 1998 Amendments, additional Unsubsidized Stafford Loan limits were established with respect to non-degree course work in the amounts of \$4,000, in connection with such course work necessary for admission to a degree granting undergraduate program, and \$5,000, in connection with such course work necessary for admission to a degree granting graduate or teaching program or to establish teaching credentials. In addition, the 1998 Amendments provide for the proration of annual Unsubsidized Stafford Loan limits with respect to programs of less than one year. The Secretary has discretion to raise these limits to accommodate highly specialized or exceptionally expensive courses of study. Effective July 1, 1996, aggregate loan limits for Subsidized and Unsubsidized Stafford Loans were raised to \$189,125 for students pursuing degrees in the health professions field, subject to subsequent regulatory modification.

*Repayment.* Generally, repayment of principal on a Stafford Loan does not commence while a student remains a Qualified Student, but begins upon expiration of the applicable Grace Period, as described below. Such Grace Periods may be waived by borrowers. The Higher Education Act currently requires minimum annual payments of \$600, including principal and interest, unless the borrower and the lender agree to lesser payments. The Higher Education Act currently requires lenders to offer and to allow the borrower to select among the following repayment plans: (i) a standard repayment plan with fixed payments scheduled over a period of not more than 10 years; (ii) a graduated repayment plan with graduated payments scheduled over a period of not more than 10 years; (iii) an income-sensitive plan with income-sensitive payments that are not less than the amount of interest due scheduled over a period of not more than 10 years; and (iv) with respect to first-time borrowers after October 7, 1998 with loan amounts in excess of \$30,000, an extended repayment plan with fixed or graduated payments scheduled over a period of not to exceed 25 years. The Higher Education Act further requires that lenders notify all borrowers of the availability of income-sensitive repayment through loan consolidation and permits student borrowers to change repayment plans annually.

Pursuant to the Federal Teacher Loan Forgiveness Program, the Secretary will assume the repayment obligation of up to \$5,000 in principal and interest of Stafford Loans, or the outstanding Stafford Loan portion of FFEL Consolidation Loans, made on or after October 1, 1998 to any new borrower, including any borrower who has no outstanding loan balance on the date such loan is made, who has been employed as a full-time teacher for 5 consecutive complete academic years at low-income schools that meet specified criteria and who is not in default on a loan for which the borrower seeks forgiveness.

*Grace Periods, Deferment Periods, Forbearance Periods.* Repayment of principal on a Stafford Loan must generally commence following a period of (a) not less than 9 months or more than 12 months (with respect to loans for which the applicable interest rate is 7 percent per annum), or (b) not more than 6 months (with respect to loans for which the applicable interest rate is 9 percent per annum or 8 percent per annum), after the borrower ceases to pursue at least a half-time course of study (each a "Grace Period"). Such 6-month period excludes any period not in excess of 3 years during which a borrower who is a member of a reserve component of the Armed Forces is called or ordered to active duty for a period of more than 30 days, including the period necessary to resume enrollment at the borrower's next available regular enrollment period. However, during certain other periods and subject to certain conditions, no principal repayments need be made, including periods when: (i) the student has returned to an eligible educational institution or is pursuing studies pursuant to an approved graduate fellowship program; (ii) the borrower is a member of the Armed Forces or a volunteer under the Peace Corps Act or the Domestic Volunteer Service Act of 1973; (iii) the borrower is at least a half-time student; (iv) when the borrower is temporarily totally disabled; (v) the borrower is unable to secure employment by reason of the care required by a dependent who is so

disabled; (vi) the borrower is pregnant, on parental leave to care for a newborn child or newly-adopted child, or is the mother of a pre-school child and is not attending a school or gainfully employed; or (vii) certain other periods of unemployment, economic hardship or qualified internships occur (each a “Deferment Period”). For new borrowers to whom loans are first disbursed on or after July 1, 1993, payment of principal may be deferred only while the borrower: (i) is at least a half-time student, is in an approved graduate fellowship program or is enrolled in a rehabilitation program; or (ii) subject in each instance to a maximum deferment of three years, when the borrower is seeking but unable to find full-time employment or when the lender determines, in accordance with regulations promulgated by the Secretary, that payment of principal will cause the borrower economic hardship. Lenders must allow periods of forbearance upon written request, renewable at twelve-month intervals, on terms agreed to in writing by parties to the loan: (i) during the borrower’s participation in certain medical or dental internships or residency programs; (ii) during periods, not in excess of three years, in which the borrower’s student loan debt burden equals or exceeds 20 percent of gross income; (iii) during periods in which the borrower is serving in a national service position for which the borrower receives a national service educational award under the National and Community Service Trust Act of 1993; and (iv) during periods in which the Secretary is paying interest subsidy payments and special allowance payments under the Armed Forces Student Loan Interest Payment Program; and may also grant administrative forbearance for periods not exceeding 60 days. Lenders may also, subject to certain regulations promulgated by the Secretary, grant a forbearance for the benefit of the borrower if both the borrower and the lender agree to the terms of the forbearance in writing. Lenders are also required to grant mandatory administrative forbearances upon notification by the Secretary that certain exceptional circumstances exist or that the geographical area where the borrower resides has been designated a disaster area by certain governmental officials.

### **Interest Subsidy Payments on Subsidized Stafford Loans**

The Secretary makes quarterly Interest Subsidy Payments in the amount of interest accruing on the unpaid principal balance of Subsidized Stafford Loans prior to the commencement of repayment or during any Deferment Period. The Higher Education Act provides that the owner of an eligible Subsidized Stafford Loan shall be deemed to have a contractual right against the United States to receive Interest Subsidy Payments in accordance with its provisions. Receipt of Interest Subsidy Payments is conditioned on the eligibility of the loan for insurance or reinsurance benefits. Such eligibility may be lost if the requirements of the federal government and the guaranty agency relating to the servicing and collection of the loans are not met.

### **Unsubsidized Stafford Loans**

The 1992 Amendments created the Unsubsidized Stafford Loan program designed for students who do not qualify for Subsidized Stafford Loans due to parental and/or student income and assets in excess of permitted amounts, or who need additional loans to supplement their Subsidized Stafford Loans. Annual loan limits are as described under “—Stafford Loans Generally — *Loan Limits*” above. In other respects, the general requirements for Unsubsidized Stafford Loans are essentially the same as those for Subsidized Stafford Loans. The interest rate and the Special Allowance Payment provisions of the Unsubsidized Stafford Loans are the same as those of the Subsidized Stafford Loans. However, the terms of the Unsubsidized Stafford Loans differ materially from Subsidized Stafford Loans in that the federal government will not make Interest Subsidy Payments and the loan limitations are determined without respect to the expected family contribution. The borrower is required to pay interest from the time such loan is disbursed or capitalize the interest until repayment begins.

The amount of periodic payments and the repayment schedule for an Unsubsidized Stafford Loan are established by assuming an interest rate equal to the applicable rate of interest at the time the repayment of the loan principal commences. At the option of the lender, the note or other written evidence of the loan may require that the amount of the periodic payment be adjusted annually or the period of repayment of principal be lengthened or shortened in order to reflect adjustments in interest rates.



## PLUS and SLS Loan Programs

The Higher Education Act authorizes PLUS Loans to be made to parents of eligible dependent students and, prior to July 1, 1994, authorized SLS Loans to be made to certain categories of students. Only parents who do not have an adverse credit history are eligible for PLUS Loans originated after July 1, 1993. Commencing July 1, 1994, the SLS Loan program has been replaced by the Unsubsidized Stafford Loan program, with annual loan limits in the merged program equal to the combined limits of the two programs prior to the merger. The basic provisions applicable to PLUS and SLS Loans are similar to those of Stafford Loans with respect to the federal insurance and reinsurance on the loans. However, PLUS Loans and SLS Loans differ from Subsidized Stafford Loans, particularly because borrowers need not demonstrate Unmet Need to qualify for PLUS or SLS Loans and because Interest Subsidy Payments are not available and Special Allowance Payments are more restricted under the PLUS and SLS Programs.

*Loan Limits.* SLS Loan limits for loans disbursed during the period from July 1, 1993 through July 1, 1994 depend upon the class year of the student and the length of the academic year. The annual loan limit for SLS Loans first disbursed during such period ranges from \$4,000 for first and second year undergraduate borrowers to \$10,000 for graduate borrowers, with a maximum aggregate amount of \$23,000 for undergraduate borrowers, and \$73,000 for graduate and professional borrowers. The only limit on the annual and aggregate amounts of PLUS Loans first disbursed on or after July 1, 1993 is the cost of the student's education less other financial aid received, including scholarship, grants and other student loans. PLUS Loans and SLS Loans disbursed during the period from October 17, 1986 through July 1, 1993 were limited to \$4,000 per academic year with a maximum aggregate amount of \$20,000.

*Interest.* Interest rates on PLUS Loans and SLS Loans depend upon the date of issuance of the loan and the period of enrollment. For PLUS Loans issued on or after October 1, 1981, for periods of educational enrollment beginning prior to July 1, 1987, the applicable rate of interest is either 12 percent or 14 percent per annum. A variable interest rate applies to PLUS Loans and SLS Loans made and disbursed on or after July 1, 1987, or made to refinance fixed-rate PLUS Loans. The variable interest rate for PLUS Loans and SLS Loans made and disbursed during the period from July 1, 1987 through September 30, 1992 is capped at a maximum rate of 12 percent per annum and is reset each July 1 and is effective through June 30 of the following year, at the weekly average one-year constant maturity Treasury yield, as published by the Board of Governors of the Federal Reserve System, for the last calendar week ending on or before such June 26 plus 3.25 percent. The variable interest rate for PLUS Loans and SLS Loans first disbursed during the period from October 1, 1992 through June 30, 1998 is based on the same bond equivalent rate of one-year constant maturity Treasury yield as PLUS Loans and SLS Loans disbursed before October 1, 1992, except that 3.10 percent is added to the bond equivalent rate of one-year constant maturity Treasury yield, with a maximum rate of 11 percent per annum for SLS Loans, and a maximum rate of 10 percent per annum for PLUS Loans. The maximum rate applicable to PLUS Loans disbursed during the period from July 1, 1994 through June 30, 1998 is 9 percent per annum. PLUS Loans made during the period from July 1, 1998 through June 30, 2006 bear interest at a rate equivalent to the 91-Day T-Bill Rate plus 3.1 percent, with a maximum rate of 9 percent. PLUS loans first disbursed on or after July 1, 2006 will bear interest at a fixed rate of 7.9 percent per annum. Special Allowance Payments are available on variable rate PLUS Loans and SLS Loans only if, at the time of computation, the rate determined by the formula above would exceed the applicable allowed maximum described above.

*Repayment, Deferments.* SLS borrowers have the option to defer commencement of repayment of principal until the commencement of repayment of Subsidized Stafford Loans. Otherwise, repayment of principal of PLUS Loans and SLS Loans is required to commence no later than 60 days after the date of disbursement of such loan, subject to certain deferral provisions. The deferral provisions that apply to PLUS Loans are more limited than those that apply to Subsidized Stafford Loans. Repayment of principal, however, may be deferred during certain periods specified under the Higher Education Act. Further, although Interest Subsidy Payments are not available for such deferments, interest may be capitalized during such periods upon agreement of the lender and borrower. Maximum loan repayment periods and minimum payment amounts are the same as for Stafford Loans.

A borrower may refinance all outstanding PLUS Loans or SLS Loans under a single repayment schedule for principal and interest, with the new repayment period calculated from the date of repayment of the most recent included loan. The interest rate of such refinanced loan shall be the weighted average of the rates of all loans being

refinanced. A second type of refinancing enables an eligible lender to reissue a PLUS Loan or SLS Loan that was initially originated at a fixed rate prior to July 1, 1987 in order to permit the borrower to obtain the variable interest rate available on PLUS Loans or SLS Loans on and after July 1, 1987. If a lender is unwilling to refinance the original PLUS Loan or SLS Loan, the borrower may obtain a loan from another lender for the purpose of discharging the loan and obtaining a variable interest rate.

### **The Consolidation Loan Program**

The Higher Education Act authorizes a program under which certain borrowers may consolidate their various federal education loans into a single FFEL Consolidation Loan insured and reinsured on a basis similar to that of Stafford Loans. FFEL Consolidation Loans may be made in an amount sufficient to pay outstanding principal, unpaid interest and late charges on all federally insured or reinsured FFELP Loans selected by the borrower, as well as loans made pursuant to various other student loan programs, including the Federal Direct Student Loan Program, and which may have been made by different lenders. Under this program, a lender may make a FFEL Consolidation Loan to an eligible borrower at the request of the borrower if the lender holds an outstanding loan of the borrower, if the borrower certifies that he has been unable to obtain a FFEL Consolidation Loan with income-sensitive terms from the holders of the outstanding loans made to the borrower or if the borrower has multiple FFELP Loans with different holders.

FFEL Consolidation Loans are available to borrowers in repayment status or in a Grace Period preceding repayment. For applications received prior to January 1, 1993, the borrower must not be delinquent by more than 90 days on any student loan payment. For applications received on or after January 1, 1993, delinquent or defaulted borrowers are eligible to obtain FFEL Consolidation Loans if they have made arrangements to repay the defaulted loan which are satisfactory to the holder. For applications received on or after January 1, 1993, married couples who agree to be jointly and severally liable will be treated as one borrower for purposes of loan consolidation eligibility.

FFEL Consolidation Loans for which the application was received before November 13, 1997 bear interest at a rate equivalent to the weighted average of the interest rates on the loans consolidated, rounded upward to the nearest whole percentage; for such FFEL Consolidation Loans originated prior to July 1, 1994 a minimum rate of 9 percent applies. FFEL Consolidation Loans for which the application was received during the period from November 13, 1997 through September 30, 1998 bear interest at a rate equivalent to the 91-Day T-Bill Rate plus 3.1 percent, with a maximum rate of 8.25 percent. FFEL Consolidation Loans for which the application is received on or after October 1, 1998 bear interest at a rate equivalent to the weighted average of the interest rates on the loans consolidated, rounded upwards to the nearest one-eighth of 1 percent, with a maximum rate of 8.25 percent. The repayment schedules for FFEL Consolidation Loans will not exceed: (i) 10 years for loans less than \$7,500; (ii) 12 years for loans greater than or equal to \$7,500, but less than \$10,000; (iii) 15 years for loans greater than or equal to \$10,000, but less than \$20,000; (iv) 20 years for loans greater than or equal to \$20,000, but less than \$40,000; (v) 25 years for loans greater than or equal to \$40,000, but less than \$60,000; and (vi) not more than 30 years for loans equal to or in excess of \$60,000. The Secretary makes Interest Subsidy Payments on FFEL Consolidation Loans: (i) for which applications were received during the period from January 1, 1993 through August 9, 1993; (ii) which consolidate only Subsidized Stafford Loans and for which applications were received by lenders during the period from August 10, 1993 through November 12, 1997; and (iii) for which applications are received during the period from November 13, 1997 through September 30, 2004 with respect to that portion of a FFEL Consolidation Loan which repays Subsidized Stafford Loans. The borrower is eligible for certain deferments of principal and interest payments for periods similar to those for Subsidized Stafford Loans, and, subject to the foregoing, Interest Subsidy Payments are made to the eligible holder during such periods. Deferred interest payments for which Interest Subsidy Payments are not available are capitalized. Borrowers may elect to accelerate principal payments without penalty. Further, no insurance premium may be charged to a borrower and no insurance premium may be charged to a lender in connection with a FFEL Consolidation Loan. However, a fee may be charged to the lender by the guaranty agency to cover the costs of increased or extended liability with respect to a FFEL Consolidation Loan. Holders of FFEL Consolidation Loans which were first disbursed during the periods from October 1, 1993 through September 30, 1998 and on or after February 1, 1999 are required to make monthly rebate payments to the Secretary calculated on an annual basis equal to 1.05 percent of the principal plus accrued interest on such loans. Holders of FFEL Consolidation Loans which were first disbursed during the period from October 1, 1998 through January 31,

1999 are required to make such rebate payments calculated on an annual basis equal to .62 percent of the principal plus accrued interest on such loans.

Repayment of Consolidation Loans begins 60 days after discharge of all prior loans that are consolidated. Repayment schedule options must include the establishment of graduated and income sensitive repayment plans, subject to certain limits applicable to the sum of the Consolidation Loan and the amount of the borrower's other eligible student loans outstanding. All eligible loans of a borrower selected for consolidation are discharged in the consolidation process and a new loan is issued.

### **Special Allowance Payments**

The Higher Education Act provides for Special Allowance Payments to be made by the Secretary to eligible lenders holding FFELP Loans. The rates for Special Allowance Payments are based on formulas that differ according to the type of loan (Stafford Loan, PLUS Loan, SLS Loan or FFEL Consolidation Loan), the date the loan was originally made or insured and the type of funding used by the holder to finance such loan (tax-exempt or taxable). Generally, the sum of the stated interest on the loan and the applicable Special Allowance Payment for a quarter will be a statutorily specified number of percentage points (the "SAP Spread") above the 91-Day T-Bill Rate for that quarter, with respect to loans first disbursed on or prior to December 31, 1999, and above the CP Rate, with respect to loans first disbursed during the period from January 1, 2000 through June 30, 2006.

The SAP Spread applicable to FFELP Loans originated prior to October 1, 1992 was 3.5 or 3.25 percent. The SAP Spread applicable to Stafford Loans originated: (i) during the period from October 1, 1992 through June 30, 1995 is 3.1 percent; (ii) during the period from July 1, 1995 through June 30, 1998, during in-school, grace and deferment periods, is 2.5 percent, and, otherwise, is 3.1 percent; (iii) during the period from July 1, 1998 through December 31, 1999, during in-school, grace and deferment periods, is 2.2 percent and, otherwise, is 2.8 percent; and (iv) during the period from January 1, 2000 through June 30, 2006, during in-school, grace and deferment Periods, is 1.74 percent and, otherwise, is 2.34 percent. The SAP Spread applicable to PLUS and SLS Loans originated: (i) during the period from October 1, 1992 through December 31, 1999 is 3.1 percent; and (ii) during the period from January 1, 2000 through June 30, 2006 is 2.64 percent. The SAP Spread applicable to FFEL Consolidation Loans originated: (i) during the period from October 1, 1992 through December 31, 1999 is 3.1 percent; and (ii) during the period from January 1, 2000 through June 30, 2006 is 2.64 percent.

Special Allowance Payments are generally payable, with respect to variable rate FFELP Loans to which a maximum borrower interest rate applies, only when such maximum rate is in effect. See "—Legislative and Administrative Matters — *Certain Recent Developments.*" The rate of Special Allowance Payments is subject to reduction by the amount of certain origination fees charged to borrowers and may be reduced as a result of certain federal budget deficit reduction measures. Notwithstanding the foregoing, Special Allowance Payments applicable to certain loans made or purchased with funds obtained from the issuance of tax-exempt obligations which were originally issued prior to October 1, 1993, are reduced by approximately one-half, subject to certain minimums provided in the Higher Education Act. These minimum Special Allowance Payment rates effectively insure an overall minimum return of 9.5 percent on such loans. The Secretary is required, however, to reduce the total amount of Interest Subsidy Payments and Special Allowance Payments with respect to any loan for which the first disbursement was made on or after October 1, 1993 by an amount equivalent to .50 percent of the principal amount of such loan.

The Higher Education Act provides that a holder of a qualifying loan who is entitled to receive Special Allowance Payments has a contractual right against the United States, during the life of the loan, to receive those Special Allowance Payments. Receipt of Special Allowance Payments, however, is conditioned on the eligibility of the loan for federal insurance or reinsurance benefits. Such eligibility may be lost due to violations of the federal or guaranty agency regulations specifying servicing and collection of the loan in the event of delinquency.

## **Federal Insurance and Reinsurance and Reimbursement of Guaranty Agencies**

A loan made under the Federal Family Education Loan Program is considered to be in default for purposes of the Higher Education Act when the borrower fails to make an installment payment when due, or to comply with other terms of the loan, and if the failure persists for 270 days beyond the payment due date, in the case of a loan repayable in monthly installments, or for 330 days beyond the payment due date, in the case of a loan repayable in less frequent installments. FFELP Loans that became delinquent prior to October 1, 1998 were considered in default if remaining unpaid after 180 days, in the case of a loan repayable in monthly installments, or after 240 days, in the case of a loan repayable in less frequent installments.

If the loan in default is covered by federal loan insurance in accordance with the provisions of the Higher Education Act, the Secretary is to pay the insurance beneficiary the amount of the loss sustained thereby, upon notice and determination of such amount, within 90 days of such notification, subject to reduction as described below.

The Higher Education Act provides that, subject to compliance with the Higher Education Act, the full faith and credit of the United States is pledged to the payment of insurance claims. It further provides that guaranty agencies shall be deemed to have a contractual right against the United States to receive reinsurance in accordance with its provisions. Federal reinsurance and insurance payments for defaulted loans are paid from the Student Loan Insurance Fund established under the Higher Education Act. The Secretary is authorized, to the extent provided in advance by appropriations acts, to issue obligations to the Secretary of the Treasury to provide funds to make such federal payments. In addition, the Higher Education Act provides that if the Secretary determines that a guaranty agency is unable to meet its insurance obligations, holders of loans may submit insurance claims directly to the Secretary until such time as the obligations are transferred to a new guaranty agency capable of meeting such obligations or until a successor guaranty agency assumes such obligations and further provide that the Secretary will pay to holders the full insurance obligations of such guaranty agency, in accordance with requirements which are no more stringent than those of such guaranty agency. There can be no assurance, however, that the Secretary will ever make such a determination or will do so in a timely manner. The Higher Education Act also provides that the Secretary is authorized, on terms and conditions satisfactory to the Secretary, to make advances to a guaranty agency in order to assist the guaranty agency in meeting its immediate cash needs and to ensure uninterrupted payment of default claims by lenders.

If the loan is guaranteed by a guaranty agency, the eligible lender is reimbursed by the guaranty agency pursuant to agreements for guarantee. Such agreements typically provide for reimbursement of the unpaid principal balance of the loan plus accrued unpaid interest on any loan defaulted so long as the eligible lender has properly serviced such loan. Pursuant to most agreements for guarantee between a guaranty agency and the originator of the loan, any eligible holder of a loan insured by such guaranty agency is entitled, subject to the preceding sentence, to reimbursement from such guaranty agency for 98 percent of any proven loss incurred with respect to defaulted claims and 100 percent of any proven loss incurred with respect to claims relative to certain lender-of-last-resort-loans or claims resulting from bankruptcy, death, disability, false certification or school closure.

A holder of a loan is required to exercise due care and diligence in the servicing of the loan and to utilize practices that are at least as extensive and forceful as those utilized by financial institutions in the collection of other consumer loans. If a guaranty agency has probable cause to believe that the holder has made misrepresentations or failed to comply with the terms of its agreement for guarantee, the guaranty agency may take reasonable action including withholding of payments or requiring reimbursement of funds. The guaranty agency may also terminate the agreement for cause upon notice and hearing. Holders are required to request preclaims assistance from the guaranty agency in order to attempt to cure the delinquency. Holders may submit claims to the guaranty agency with respect to loans that default. At the time of payment of insurance benefits, the holder must assign to the guaranty agency all rights accruing to the holder under the note evidencing the loan.

Under the Higher Education Act, the Secretary enters into a guaranty agreement and an annually renewable supplemental guaranty agreement with each guaranty agency that provides for federal reinsurance for amounts paid to eligible lenders by the guaranty agency with respect to defaulted loans. Pursuant to such agreements, the Secretary is to reimburse a guaranty agency for a percentage of default losses and for 100 percent of the amounts expended in connection with a claim with respect to loans made under a qualifying lender-of-last-resort program or

a claim resulting from the death, discharge in bankruptcy, or total and permanent disability of a borrower, the death of a student whose parent is the borrower of a PLUS Loan, or claims by borrowers who are unable to complete the programs in which they are enrolled due to school closure or whose borrowing eligibility was falsely certified by the eligible institution. Such claims are not included in calculating a guaranty agency's claims rate experience for purposes of reducing federal reinsurance payments received by guaranty agencies as described in the following paragraphs.

Guaranty agencies are required to satisfy due diligence requirements prescribed by regulations with respect to defaulted loans. The Secretary may require repayment of reinsurance payments, and may require other remedial action, including the withholding of payments, imposition of fines and suspension or termination of agreements, in response to a guaranty agency's failure to comply with applicable regulations.

Under the Higher Education Act, reimbursement by the Secretary of a guaranty agency for any amounts paid to satisfy claims with respect to loans which are not made under a qualified lender-of-last-resort program and which do not result from death, bankruptcy, disability, school closure or false certification is subject to reduction as described in the following paragraphs.

The original principal amount of loans guaranteed by a guaranty agency that are in repayment for purposes of computing reimbursement payments to a guaranty agency means the original principal amount of all loans guaranteed by a guaranty agency less: (i) guarantee payments on such loans; (ii) the original principal amount of such loans which have been fully repaid; and (iii) the original amount of such loans for which the first principal installment payment has not become due.

The amount of such insurance or reinsurance payments is subject to reduction based upon the annual claims rate of the guaranty agency, calculated to equal the amount of federal reinsurance as a percentage of the original principal amount of guaranteed loans in repayment on the last day of the prior fiscal year. The formula generally applicable under the 1998 Amendments is as follows:

<u>Claims Rate</u>	<u>Federal Payment</u>
0 percent up to 5 percent	95 percent of claim amounts
Over 5 percent to 9 percent	95 percent of claims up to 5 percent, 85 percent of claims of over 5 percent
Over 9 percent	95 percent of claims up to 5 percent, 85 percent of claims greater than 5 percent to 9 percent, and 75 percent of claims greater than 9 percent

The claims experience is not accumulated from year to year, but is determined solely on the basis of claims in any one federal fiscal year compared with the original principal amount of loans in repayment at the end of the prior federal fiscal year.

Notwithstanding the foregoing the Secretary will reimburse a guaranty agency: (i) with respect to loans that are transferred from an insolvent guaranty agency pursuant to a plan approved by the Secretary at rates that are equivalent to those set forth above plus 5 percent; and (ii) with respect to loans made pursuant to a qualifying lender-of-last-resort program at a rate of 100 percent of claim amounts.

The 1998 Amendments authorized the retention by guaranty agencies for general operating purposes of default aversion fees equivalent to 1 percent of the total unpaid principal and accrued interest on FFELP Loans on which default aversion assistance has been requested and that are subsequently brought into current repayment status. The 1998 Amendments further authorized the payment to guaranty agencies of loan processing and issuance fees of .65 percent, with respect to FFELP Loans originated during the period from October 1, 1998 through September 30, 2003, and of .40 percent, thereafter. The 1998 Amendments further authorized the payment to guaranty agencies of account maintenance fees of .12 percent annually with respect to original principal outstanding of FFELP Loans during the period from October 1, 1998 through September 30, 2000 and of .10 percent annually with respect to the original principal amount of FFELP Loans during the period from October 1, 2000 through September 30, 2003.

Guaranty agencies are required to maintain specific reserve fund levels. If the agency fails to achieve the minimum reserve level in any of two consecutive years, if the agency's federal reimbursements are reduced to 85 percent or if the Secretary determines the agency's administrative or financial condition jeopardizes its continued ability to perform its responsibilities, the Secretary may require the agency to submit and implement a management plan to address the deficiencies. The Secretary may terminate the agency's agreements with the Secretary if the agency fails to submit the required plan, or fails to improve its administrative or financial condition substantially, or if the Secretary determines the agency is in danger of financial collapse. In such event, the Secretary is authorized to undertake specified actions to assure the continued payment of claims, including the transfer of guarantees to another agency, or transfer of guarantees to the Department itself. The Higher Education Act allows the Secretary to terminate a guaranty agency's agreement if the Secretary determines that termination is necessary to protect the federal financial interest, or to ensure the continued availability of loans to student or parent borrowers. The Secretary is authorized to provide the guaranty agency with additional advance funds with such restrictions on the use of such funds as are determined appropriate by the Secretary in order to meet the immediate cash needs of the guaranty agency, ensure the uninterrupted payment of claims, or ensure that the guaranty agency will make loans as the lender-of-last-resort.

The Higher Education Act provides that if the Secretary has terminated or is seeking to terminate a guaranty agency's agreement, or has assumed a guaranty agency's functions, notwithstanding any other provision of law: (i) no state court may issue an order affecting the Secretary's action with respect to that guaranty agency; (ii) any contract entered into by the guaranty agency with respect to the administration of the agency's reserve funds or assets acquired with reserve funds shall provide that the contract is terminable by the Secretary upon 30 days' notice to the contracting parties if the Secretary determines that such contract includes an impermissible transfer of funds or assets or is inconsistent with the terms or purposes of this law; and (iii) no provision of state law shall apply to the actions of the Secretary in terminating the operations of the guaranty agency. Finally, notwithstanding any other provision of law, the 1993 Amendments provide that the Secretary's liability for any outstanding liabilities of a guaranty agency (other than outstanding student loan guarantees under Part D of Title IV of the Higher Education Act), the functions of which the Secretary has assumed, shall not exceed the fair market value of the reserves of the guaranty agency, minus any necessary liquidation or other administrative costs.

The Higher Education Act contains provisions to the effect that, notwithstanding any other provision of law, a substantial portion of the reserve funds of the guaranty agencies, and any assets purchased with such portion of such reserve funds, regardless of who holds or controls the reserves or assets, are the property of the United States to be used in the operation of the FFEL Program or as otherwise provided by federal legislation. Such portion of such reserves will be required to be maintained by each guaranty agency to pay lender claims, to fund default aversion fees and, subject to certain restrictions, to fund guaranty agency operating costs on a no-interest loan basis. The Higher Education Act grants the Secretary broad powers over the administration and application of such portion of such reserves and, under certain conditions, of all guaranty agency reserves.

The Balanced Budget Act of 1997 (Pub. L. 105-33) (the "Balanced Budget Act") required the Secretary to recall \$1 billion in reserve funds from guaranty agencies on September 1, 2002. The 1998 Amendments required the Secretary to recall an additional \$250 million in reserve funds from guaranty agencies by federal fiscal year 2007. Each of the Balanced Budget Act and the 1998 Amendments contained detailed provisions as to the allocation of amounts to be so recalled among guaranty agencies. In addition, the 1998 Amendments required the Secretary to transfer all funds in the Student Loan Insurance Fund as of October 7, 1998 to the Treasury. There can be no assurance that future legislation will not require the recall and transfer of substantially all federal funds, including the federal portion of guaranty agency reserve funds, which are immediately available to fund guaranty agency and federal payment obligations arising in connection with the FFEL Program.

### **Education Loans Generally Not Subject to Discharge in Bankruptcy**

Under the United States Bankruptcy Code, education loans are not generally dischargeable. Title 11 of the United States Code at Section 523(a)(8) provides as follows:

(a) A discharge under Section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt -

(8) for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents.

### **Servicer Provisions and Third-Party Servicer Requirements**

On April 29, 1994, the Department published regulations amending the Student Assistance General Provisions and FFEL Program regulations that, among other things, establish requirements governing contracts between holders of FFELP Loans and third-party servicers, establish standards of administrative and financial responsibility for third-party servicers that administer any aspect of a guaranty agency's or lender's participation in the FFEL Program, and establish sanctions for third-party servicers.

Under these regulations, a third-party servicer is jointly and severally liable with its client lenders, guaranty agencies and educational institutions, as applicable, for liability to the Department arising from the servicer's violation of applicable requirements. In addition, if a servicer fails to meet standards of financial responsibility or administrative capability included in the new regulations, or violates other FFEL Program requirements, the new regulations authorize the Department to fine the servicer or limit, suspend, or terminate the servicer's eligibility to contract to service Student Loans. The effect of such a limitation, suspension, or termination on a servicer's eligibility to service loans already on its system, or to accept new loans for servicing under existing contracts is unclear. No assurance exists that the Corporation will not be held liable by the Department for liabilities arising out of its FFEL Program activities for the Corporation or other client lenders, or that its eligibility will not be limited, suspended, or terminated in the future. If the Corporation were so held liable or its eligibility limited, suspended, or terminated, its ability to properly service Student Loans and to satisfy its obligations with respect thereto may be adversely affected.

The 1998 Amendments provide that an eligible lender or guaranty agency that contracts with another entity to perform any of its functions with respect to the FFEL Program or otherwise delegates the performance of such functions shall not be relieved of its duty to comply with the requirements of the Higher Education Act and shall monitor the activities of such other entity for compliance with such requirements.

### **Loan Origination and Servicing Procedures Applicable to Student Loans**

The Higher Education Act, including the implementing regulations thereunder, imposes specified requirements, guidelines and procedures with respect to originating and servicing FFELP Loans. Generally, those procedures require that completed loan applications be processed, a determination of whether an applicant is an eligible borrower under applicable standards be made, the borrower's responsibilities under the loan be explained to him or her, the promissory note evidencing the loan be executed by the borrower and then that the loan proceeds be disbursed in a specified manner by the lender. After the loan is made, the lender must establish repayment terms with the borrower, properly administer deferrals and forbearance and credit the borrower for payments made thereon. If a borrower becomes delinquent in repaying a loan, a lender or a servicing agent must perform certain collection procedures (primarily telephone calls and demand letters) that vary depending upon the length of time a loan is delinquent. Numerous federal and state consumer protection laws and related regulations impose substantial requirements upon lenders and servicers involved in consumer finance. Also, some state laws impose finance charge ceilings and other restrictions on certain consumer transactions and require contract disclosures in addition to those required under federal law. These requirements impose specific statutory liabilities upon lenders who fail to comply with their provisions. In certain circumstances, the Corporation may be liable for certain violations of consumer protection laws that apply to the Financed Student Loans, either as assignee or as the party directly responsible for obligations arising after the transfer.

### **Federal Direct Student Loan Program**

Under the Federal Direct Student Loan Program (the "FDSL Program") established by the 1993 Amendments, a variety of direct federal loans with terms and conditions generally similar to those available under the FFEL Program may be obtained by students, or parents of students, attending participating Institutions of Higher

Education (“IHE”) through the applicable IHE or through an alternative originator designated by the Secretary, without application to an outside lender. The FDSL Program is funded and administered by the Secretary. The FDSL Program provides for a variety of repayment plans from which borrowers may choose, including repayment plans based on income. In addition, if a borrower is unable to obtain a FFEL Consolidation Loan with income sensitive repayment terms acceptable to the borrower from the holders of the borrower’s outstanding FFELP Loans (that are selected for consolidation), or from any other lender, including the Student Loan Marketing Association, the 1993 Amendments authorize the Secretary to offer the borrower a consolidation loan with income sensitive terms under the FDSL Program. The 2002 Amendments provide that the interest rate formulas for loans made under the FDSL Program are extended to loans disbursed before July 1, 2006. Interest rates for loans disbursed on or after July 1, 2006 have been changed to fixed rates.



## **Appendix B**

### **Definitions of Certain Terms**

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**DEFINITIONS OF CERTAIN TERMS**

The following are definitions of certain terms used in this Official Statement. Capitalized terms that are not otherwise defined herein shall have the meanings given to those terms in the Resolutions.

“Account” means any of the special trust accounts created and established by, or pursuant to, the Resolutions.

“Accountant” or “Auditor” means any independent certified public accountant, or a firm of those accountants, duly licensed to practice and practicing as such under the laws of the Commonwealth, selected by the Corporation, who is independent and not under the domination or control of the Corporation and who does not have any substantial interest, direct or indirect, in the Corporation, but who may be regularly retained to make annual or similar audits of the books or records of the Corporation.

“Act” means Sections 164A.010 to 164A.240, inclusive, of the Kentucky Revised Statutes, as heretofore or hereafter amended.

“Additional Obligations” means any Obligations other than the initial two Series of Obligations which shall be authenticated and delivered on original issuance pursuant to the Resolutions or thereafter authenticated or delivered in lieu of or in substitution for any such Obligation pursuant to the Resolutions.

“Applicable Law” means: (i) with respect to Student Loans originated pursuant to the Federal Family Education Loan Program, the Act and the Higher Education Act; and (ii) with respect to any other Student Loans, the Act, any other state or federal law applicable thereto or any regulation promulgated thereunder.

“ARCs” means any Subseries of the Senior Series 2003A Bonds bearing interest at an Auction Rate.

“Authorized Officer” means the Chairman, Secretary-Treasurer, Executive Director, Chief Executive Officer or Chief Financial Officer of the Corporation, and any other of its directors, officers, agents or employees duly authorized by the by-laws or by a resolution of the Corporation to perform the act or sign the document in question.

“Beneficial Owner” means the purchaser of a beneficial ownership interest in any Bond.

“Bonds” means debt obligations of the Corporation, whether or not so designated, other than Notes or Other Obligations, issued to finance or refinance the making or purchase of Student Loans by the Corporation pursuant to the Resolutions, which mature no later than thirty years from the date of original issuance of such Bonds.

“Business Day” means, with respect to each Series of Obligations, any day on which banks located in none of: (i) the Commonwealth of Kentucky; (ii) the city in which the principal corporate trust office of each Fiduciary applicable to such Series of Obligations; (iii) the city in which the principal offices of the Corporation; and (iv) the city in which the principal offices of each Obligation Facility Provider applicable to such Series are located are required or authorized by law to remain closed and on which the New York Stock Exchange is not closed, except as otherwise provided with respect to any Series by the Series Resolution authorizing such Series.

“Cash Flow Projection” means a schedule prepared on behalf of the Corporation by a nationally recognized investment banking firm or other entity selected by the Corporation and approved in writing by the Rating Agencies receiving such Cash Flow Projection which: (i) sets forth, through the last final maturity of any Series of Outstanding Obligations (or such shorter period as shall be acceptable to the Rating Agencies), (A) all anticipated Revenues, (B) the application of all such Revenues in accordance with the Resolutions and (C) the resulting balances for each period for which prepared and on a cumulative basis; and (ii) evidences that Revenues and other monies available under the Resolutions will be sufficient to pay all debt service on the Obligations when due and to make all other payments required by the terms of the Resolutions. Each Cash Flow Projection shall be based on the

assumptions used in the cash flow projections delivered to the Rating Agencies at the time of issuance of the most recently issued Series of Obligations (or such other assumptions as may be proposed by the Corporation and acceptable to the Rating Agencies) and upon actual Account balances.

“Certificate” means: (i) a signed document either attesting to or acknowledging the circumstances, representations or other matters therein stated or set forth or setting forth matters to be determined pursuant to the Resolutions; or (ii) the report of an accountant as to audit or other procedures called for by the Resolutions.

“Class” means all Obligations having the same priority of claim as to payment under the Resolutions.

“Code” means the Internal Revenue Code of 1986, as amended from time to time. Each reference to a section of the Code herein shall be deemed to include the United States Treasury Regulations, including temporary and proposed regulations, relating to such section which are applicable to the Obligations or the use of the proceeds thereof. A reference to any specific section of the Code shall be deemed also to be a reference to the comparable provisions of any enactment which supersedes or replaces the Code thereunder from time to time.

“Commonwealth” means the Commonwealth of Kentucky.

“Corporation” means the Kentucky Higher Education Student Loan Corporation, an independent *de jure* municipal corporation and political subdivision of the Commonwealth, created and existing under and pursuant to the Act, or any body, agency, authority or instrumentality of the Commonwealth that shall hereafter succeed to the powers, duties and functions of the Corporation.

“Costs of Issuance” means all items of expense, directly or indirectly payable or reimbursable by or to the Corporation and related to the authorization, sale and issuance of Obligations, including, but not limited to, printing costs, costs of preparation and reproduction of documents, filing and recording fees, initial fees and charges of any Fiduciary or of its counsel, legal fees and charges, fees and expenses of underwriters, fees and disbursements of consultants and professionals, costs of credit ratings, fees and charges for preparation, execution, transportation and safekeeping of Obligations, costs and expenses of refunding, premiums, fees, expenses or other similar charges payable to any Obligation Facility Provider (other than Reimbursement Obligations or Other Obligations) or a Swap Provider (other than Swap Payments or Other Obligations), financing charges, accrued interest with respect to the initial investment of proceeds of Obligations, and any other cost, charge or fee in connection with the original issuance of Obligations.

“Counsel’s Opinion” means a written opinion signed by Hawkins, Delafield & Wood or by another attorney or firm of attorneys of recognized standing in the field of law relating to municipal, state and public agency financing, selected by the Corporation and reasonably satisfactory to the Trustee and any applicable Obligation Facility Provider.

“Debt Service Reserve Account” means the special trust account so denominated established pursuant to the Resolutions.

“Defeasance Securities” means obligations described in paragraph (1) of the definition of Investment Securities included hereunder.

“DTC” means The Depository Trust Company (a limited purpose trust company), New York, New York.

“Earnings Account” means the special trust account so denominated established pursuant to the Resolutions.

“Eligible Lender” means the Kentucky Higher Education Assistance Authority, a *de jure* political subdivision of the Commonwealth of Kentucky and the Corporation and all other entities described as eligible lenders in the Higher Education Act which have in force a contract with a Guarantee Agency providing for loan guarantees to be issued by a Guarantee Agency to the subject lender under the Higher Education Act and the Act.

“Event of Default” means any of the events specified in the Resolutions.

“Excess Coverage” means, as of any date of calculation, the condition under which the sum of the value of (a) the Loans (valued as provided in the Resolutions) credited to the Loan Account and (b) all cash and Investment Securities held in the Accounts (valued as set forth in the Resolutions, plus accrued interest, but excluding amounts irrevocably set aside to pay particular Obligations pursuant to the Resolutions and excluding amounts on deposit in the Rebate Account) shall be at least equal to each of the following three sums: (x) 106% of the sum of the principal of and accrued interest on all Outstanding Senior Obligations plus all accrued but unpaid Program Expenses; (y) 104% (or, subsequent to delivery to the Trustee of a Rating Affirmation addressing such change, 103%) of the sum of the principal of and accrued interest on all Outstanding Senior Obligations and Senior Subordinate Obligations plus all accrued but unpaid Program Expenses; and (z) 103% (or, subsequent to delivery to the Trustee of a Rating Affirmation addressing such change, 102%) of the sum of the principal of and accrued interest on all Outstanding Obligations plus all accrued but unpaid Program Expenses.

“Federal Family Education Loan Program” or “FFELP” means the program currently authorized by Title IV Part B of the Higher Education Act, as heretofore or hereafter amended.

“Fiduciary” means the Trustee, any Paying Agent and any such additional fiduciary as may be authorized under the Resolutions, or any or all of them as may be appropriate.

“Fiscal Year” means the fiscal year of the Corporation for general financial reporting purposes as modified from time to time. As of the date of the Resolutions the Corporation’s Fiscal Year is July 1 to June 30.

“Guaranty Agency” or “Guarantee Agency” means: (i) the Kentucky Higher Education Assistance Authority duly organized and existing pursuant to the statutory laws of the Commonwealth of Kentucky; (ii) any other guaranty agency under the Higher Education Act, subject to receipt of a Rating Affirmation; and (iii) any successor to the obligations of any such Guaranty Agency under the Higher Education Act.

“Higher Education Act” means the Higher Education Act of 1965, as amended from time to time, and the regulations promulgated thereunder.

“Holder” or “Owner”, or words of similar import, when used with reference to an Obligation means the registered owner of such Obligation.

“Investment Securities” means, with respect to any Series, except as otherwise provided by a Series Resolution authorizing such Series, any of the following (excluding, however, any interest-only obligations and any obligations acquired at prices in excess of par), if and to the extent the same are at the time legal for investment of the Corporation’s funds:

(1) (a) Direct obligations (other than an obligation subject to variation in principal repayment) of the United States of America, (b) obligations fully and unconditionally guaranteed as to timely payment of principal and interest by the United States of America or (c) obligations fully and unconditionally guaranteed as to timely payment of principal and interest by any agency or instrumentality of the United States of America when such obligations are backed by the full faith and credit of the United States of America.

(2) Federal Housing Administration debentures which are rated “Aaa” by Moody’s.

(3) Obligations of government-sponsored agencies which are not backed by the full faith and credit of the U.S. government which are rated “Aaa” by Moody’s.

(4) Unsecured certificates of deposit, time deposits, and bankers’ acceptances (having maturities of not more than 30 days) of any bank the short-term obligations of which are rated “P-1” by Moody’s.

(5) Deposits the aggregate amount of which are fully insured by the Federal Deposit Insurance Corporation (FDIC), in banks which have capital and surplus of at least \$5 million.

(6) Commercial paper (having original maturities of not more than 270 days) rated “Prime-1” by Moody’s having a current maturity at the time of acquisition of: (a) not more than 120 days, if the long-term debt of the issuer is then rated no less favorably than “AA-3” by Moody’s; (b) not more than 90 days, if the long-term debt of the issuer is then rated no less favorably than “A-1” by Moody’s; or (c) otherwise not more than 30 days.

(7) Money market funds which are rated “Aaa” by Moody’s.

(8) Repurchase agreements (“repos”) in a form acceptable to Moody’s: (a) with any bank with deposits rated at least “Aa2” by Moody’s, if the term of such repo is for less than or equal to 180 days, or with deposits rated “Aaa” by Moody’s, if the term of such repo is greater than 180 days but less than or equal to two years; or (b) with any broker-dealer with “retail customers” which has long-term debt rated at least “Aa2” by Moody’s, if the term of such repo is for less than or equal to 180 days, or rated “Aaa” by Moody’s, if the term of such repo is greater than 180 days but less than or equal to two years, which broker-dealer falls under the jurisdiction of the Securities Investors Protection Corp. (SIPC).

(9) Obligations that are: (a) direct general obligations of any state of the United States or any subdivision or agency thereof to which is pledged the full faith and credit of a state the unsecured general obligation debt of which is rated “Aa2” by Moody’s, or better, or any obligation fully and unconditionally guaranteed by any state, subdivision or agency whose unsecured general obligation debt is so rated; (b) direct, general short-term obligations of any state agency or subdivision described in (a) above and rated “Prime-1” by Moody’s; or (c) Special Revenue Bonds (as defined in the United States Bankruptcy Code) of any state, state agency or subdivision described in (a) above and rated “Aa” or better by Moody’s.

(10) Investment agreements with (1) a domestic bank the long term debt of which is rated at least “Aa2” by Moody’s or (2) a foreign bank the long-term debt of which is rated at least “Aaa” by Moody’s; provided, that, by the terms of the investment agreement: (a) interest payments are to be made to the Trustee at times and in amounts as necessary to pay debt service on the Obligations the proceeds of which are invested thereunder; (b) the invested funds are available for withdrawal without penalty or premium, at any time upon not more than seven days’ prior notice (which notice may be amended or withdrawn at any time prior to the specified withdrawal date); provided that the Trustee shall give notice in accordance with the terms of the investment agreement so as to receive funds thereunder with no penalty or premium paid; (c) the investment agreement is the unconditional and general obligation of, and is not subordinated to any other obligation of, the provider thereof; (d) a fixed guaranteed rate of interest is to be paid on invested funds and all future deposits, if any, required to be made to restore the amount of such funds to the level specified under the applicable Series Resolution; (e) the Trustee receives a Counsel’s Opinion (which opinion shall be addressed to the Corporation and each applicable Obligation Facility Provider) that such investment agreement is legal, valid, binding and enforceable upon the provider in accordance with its terms; and (f) the investment agreement must provide that if during its term (i) the provider’s rating by Moody’s is withdrawn or suspended or falls below “Aa2”, the provider must give notice of same to the Corporation and the Trustee and must within 10 days of receipt of such direction, either: (A) repay the principal of and accrued but unpaid interest on the investment, with no penalty or premium to the Corporation or Trustee; or (B) collateralize the investment agreement in a manner approved by Moody’s.

(11) Pre-refunded municipal obligations rated “Aaa” by Moody’s meeting the following requirements: (a) the municipal obligations are (i) not subject to redemption prior to maturity or (ii) the trustee has been given irrevocable instructions concerning their call and redemption and the issuer of the municipal obligations has covenanted not to redeem such municipal obligations other than as set forth in such instructions; (b) the municipal obligations are secured by cash or United States Obligations which may be applied only to payment of the principal of, interest and premium on such municipal obligations; (c) the principal of and interest on the United States Obligations (plus any cash in the escrow) has been verified by the report of independent certified public accountants to be sufficient to pay in full all principal of, interest, and premium, if any, due and to become due on the municipal obligations (“Verification”); (d) the cash or United States Obligations serving as security for the municipal obligations are held by an escrow agent or

trustee in trust for owners of the municipal obligations; (e) no substitution of a United States Obligation shall be permitted except with another United States Obligation and upon delivery of a new Verification; and (f) the cash or United States Obligations are not available to satisfy any other claims, including those by or against the trustee or escrow agent.

(12) Subject to the prior written approval of each applicable Obligation Facility Provider and to receipt by the Trustee of a Rating Affirmation, such other obligations as shall be permitted to be legal investments of the Corporation by the laws of the Commonwealth.

“Issue Date” means the date of delivery of the Senior Series 2003A Bonds.

“Loan” means any Student Loan or other loans credited to the Loan Account.

“Loan Account” means the special trust account so denominated established pursuant to the Resolutions.

“Loan Program” means the program for the financing of Student Loans established by the Corporation, as the same may be amended from time to time consistent with the Resolutions, but only to the extent that such program is financed through the issuance of Obligations or from amounts otherwise available out of the moneys and assets held or pledged pursuant to the Resolutions.

“Moody’s” means Moody’s Investors Service, Inc., its successors and assigns and if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, “Moody’s” shall be deemed to refer to any other nationally recognized securities rating agency designated by the Corporation, by notice to the Trustee, and each other Fiduciary and each applicable Obligation Facility Provider.

“Most Senior Outstanding Obligations” means, at any time: (i) if any Senior Obligations are then Outstanding, such Senior Obligations; and (ii) if no Senior Obligations are then Outstanding, the Class of Senior Subordinate Obligations or Subordinate Obligations then Outstanding having the most senior priority as to payment hereunder.

“Notes” means debt obligations of the Corporation, whether or not so designated, other than Bonds or Other Obligations, issued to finance or refinance the making or purchase of Student Loans by the Corporation or any renewal thereof issued pursuant to the Resolutions, which mature no later than five years from the date of original issuance of such Notes.

“Notional Amount” means the nonpayable or the theoretical principal amount with reference to which Swap Payments and Swap Receipts are calculated, as specified as such for each Swap in the documentation applicable thereto.

“Obligation Facility” means any insurance policy, surety agreement, letter of credit or other credit enhancement or liquidity facility entered into for the same or similar purposes, with respect to any Series of Obligations, or with respect to any Student Loans described in clause (B) of the definition thereof herein, which is delivered to the Trustee along with a Certificate of an Authorized Officer to which a Rating Affirmation is attached.

“Obligation Facility Provider” means any bank or insurance company providing an Obligation Facility with respect to a Series and any successor to such an Obligation Facility Provider.

“Obligation Facility Provider Default” means any one of the following events shall have occurred and be continuing:

(i) an Obligation Facility Provider fails to make or provide for any payment required under the Obligation Facility in accordance with its terms;

(ii) an Obligation Facility Provider (A) files any petition or commences any case or proceeding under any provision or chapter of the United States Bankruptcy Code or any other similar federal or state law relating to insolvency, bankruptcy, rehabilitation, liquidation or reorganization, (B)

makes a general assignment for the benefit of its creditors, or (C) has a final and nonappealable order for relief entered against it under the United States Bankruptcy Code or any other similar federal or state law relating to insolvency, bankruptcy, rehabilitation, liquidation or reorganization;

(iii) a court of competent jurisdiction, or other competent regulatory authority enters a final and nonappealable order, judgment or decree (1) appointing a custodian, trustee, agent or receiver for an Obligation Facility Provider or for all or any material portion of its property or (2) authorizing the taking of possession by a custodian, trustee, agent or receiver of an Obligation Facility Provider (or the taking of possession of all or any material portion of the property of an Obligation Facility Provider); or

(iv) with respect to any Series of Obligations if so provided by the Series Resolution authorizing such Series, one or more Rating Agencies reduces its rating with respect to such Obligation Facility Provider to a rating below that originally assigned to such Series by such Rating Agencies; provided, that no such reduction shall affect the rights of such Obligation Facility Provider with respect to Obligations then held by it.

“Obligations” means Bonds, Notes, Reimbursement Obligations, Swap Payments and Other Obligations issued or authorized pursuant to the Resolutions and any applicable Series Resolution.

“Operating Account” means the special trust account so denominated established pursuant to the Resolutions.

“Origination Agreement” means any agreement providing for the origination or for the origination and sale of Student Loans to be financed through application of the proceeds of any Series of Obligations.

“Other Obligations” means debt obligations of the Corporation, other than Bonds and Notes, issued to finance or refinance the making or purchase of Student Loans by the Corporation pursuant to the Resolutions, but does not include any Swap Payments or Reimbursement Obligations.

“Outstanding”, when used with reference to Obligations, means, as of any date, all Obligations theretofore or thereupon being authenticated and delivered under the Resolutions except:

(1) any Obligation cancelled by the Trustee or delivered to the Trustee for cancellation at or prior to such date;

(2) any Obligation (or portion of an Obligation) for the payment or redemption of which there have been separately set aside and held in a special trust account therefor either:

(a) moneys in an amount sufficient to effect payment of the principal or applicable Redemption Price thereof, together with accrued interest on such Obligation to the Redemption Date; or

(b) Defeasance Securities, as described in the Resolutions, in such principal amounts, of such maturities, bearing such interest and otherwise having such terms and qualifications as shall be necessary to provide moneys in an amount sufficient to effect payment when due of the principal or applicable Redemption Price of such Obligation, together with accrued interest on such Obligation to the Redemption Date; or

(c) any combination of (a) and (b) above;

provided, however, that Obligations which have been paid with proceeds of an Obligation Facility shall be deemed to continue to remain Outstanding as Reimbursement Obligation Bonds evidencing the related Reimbursement Obligation for purposes of the Resolutions and to bear interest at the rate provided in the related Obligation Facility until each applicable Obligation Facility Provider has been paid as subrogee or reimbursed under the Resolutions as evidenced by a written notice from each applicable Obligation Facility Provider delivered to the Trustee, and each applicable Obligation Facility Provider shall be deemed to be



the Owner of such Obligations to the extent of any payments thereon made by each applicable Obligation Facility Provider, but only to the extent that principal of the Obligations was so paid; or

(3) any Obligation in lieu of or in substitution for which other Obligations shall have been authenticated and delivered pursuant to the Resolutions.

“Participant” means a member of, or participant in, the Securities Depository.

“Paying Agent” means the Trustee and any bank or trust company designated as paying agent for the Obligations, and its successor or successors hereafter appointed, in the manner provided in the Resolutions.

“Person” means and includes, unless otherwise specified, any natural person, any firm, partnership, joint venture, joint stock company, trust, estate, association, unincorporated organization or corporation, or public body, government or political subdivision, and any state or federal agency.

“Program Agreement” means, with respect to any Series of Obligations, each Origination Agreement and Servicing Agreement applicable to such Series.

“Program Expenses” means all of the Corporation’s expenses in carrying out and administering its Loan Program under the Resolutions and shall include, without limiting the generality of the foregoing, salaries, origination, acquisition and servicing fees, supplies, utilities, mailing, labor, materials, office rent or mortgage payment, maintenance, furnishings, equipment, machinery and apparatus, telephone, insurance premiums, legal, accounting, management, consulting and banking services and expenses, fees and expenses of the Fiduciaries, Costs of Issuance not paid from the proceeds of Obligations, including but not limited to premiums, fees, expenses or other similar charges payable to an Obligation Facility Provider or a Swap Provider (but not including Reimbursement Obligations, Swap Payments or Termination Payments), travel, payments for pension, thrift savings, retirement, health and hospitalization and life and disability insurance benefits, all to the extent properly allocable to the Loan Program. Program Expenses may also include amounts for establishing and maintaining a six-month reserve to pay operating costs and a reasonable reserve for losses and expenses estimated to be incurred by the Corporation and amounts appropriate to reimburse the Corporation for Program Expenses paid from other sources all to the extent properly allocable to the Loan Program.

“Rating Affirmation” means, with respect to each Series, the written affirmation of each Rating Agency then maintaining a rating with respect to a Series to the effect that the actions addressed therein would not cause such Rating Agency to reduce or suspend any rating then applicable to such Series.

“Rating Agency” or “Rating Agencies” means, with respect to each Series, each of Moody’s and any other nationally recognized securities rating agency which is maintaining a rating at the request of the Corporation with respect to such Series.

“Rebate Account” means the special trust account so denominated established pursuant to the Resolutions.

“Recycling Period” means the period commencing on the Issue Date and ending on July 1, 2006, except as such period may be extended by a Certificate of an Authorized Officer accompanied by a Rating Affirmation.

“Redemption Date” means each date upon which Obligations are to be called for redemption pursuant to the Resolutions.

“Redemption Price” means, with respect to any Obligation, the principal amount thereof plus the applicable premium, if any, payable upon redemption thereof together, if not otherwise provided for in the Resolutions, with accrued but unpaid interest to the date of redemption.

“Refunding Obligations” means any Obligation authenticated and delivered on original issuance pursuant to the Resolutions some portion of the proceeds of which are applied to the payment of principal or interest of Obligations or Separately Secured Financings or thereafter authenticated and delivered in lieu of or in substitution for any such Obligation pursuant to the Resolutions.

“Registrar” means the Trustee or any other agent of the Corporation at the office of which Obligations may be presented for registration, transfer or exchange as provided in the Resolutions.

“Reimbursement Obligation” means any obligation of the Corporation to make payments to an Obligation Facility Provider in reimbursement of or as interest on (which interest may be higher than the interest rate on the related Obligation) an advance or other payment made by such Obligation Facility Provider for the purpose of paying:

- (i) the principal or Redemption Price of, or interest on, any Obligations; or
- (ii) the purchase price, plus accrued interest, if any, of any Obligations tendered pursuant to the provisions of the applicable Series Resolution,

but only to the extent the principal amortization requirements with respect to such reimbursement are equal to the amortization requirements for such related Obligations, without acceleration. Reimbursement Obligations shall not include: (i) any payments of any fees, expenses, or other similar obligations to any such provider (which payments shall be Program Expenses); or (ii) any payments pursuant to term-loan or other principal amortization requirements in reimbursement of any such advance that are more accelerated than the amortization requirements on such related Obligations (which payments shall be Other Obligations). Reimbursement Obligations may be evidenced by Bonds designated as “Reimbursement Obligation Bonds”, which may bear a higher interest rate than the rate borne by the Obligations to which they relate.

“Reserve Account Facility” means an Obligation Facility pursuant to which an amount equivalent to the Reserve Account Requirement applicable to the Senior Series 2003A Bonds is available to fund transfers from the Debt Service Reserve Account to the Revenue Account pursuant to the Resolutions.

“Reserve Account Requirement” means, with respect to the Senior Series 2003A Bonds, an amount (other than a negative amount) equal to the difference between (i) 1.46% of the aggregate Outstanding principal amount of (A) the Senior Series 2003A Bonds and (B) all Outstanding Bonds issued prior to the Senior Series 2003A Bonds and (ii) the aggregate amount of all Reserve Account Requirements then applicable to Bonds described in the immediately preceding clause (i)(B); provided, that such Reserve Account Requirement may be reduced by a Supplemental Resolution authorizing the issuance of Bonds adopted subsequent to the Series 2003A-1 and Series 2003A-2 Bond Resolution or by delivery to the Trustee of a Certificate of an Authorized Officer describing the reduced Reserve Account Requirement accompanied by a Rating Affirmation; and further provided, that such Reserve Account Requirement shall remain, in any event, subject to a \$500,000 overall Debt Service Reserve Account minimum aggregate requirement.

“Resolutions” means the 1997 General Bond Resolution adopted by the Corporation on May 9, 1997, as heretofore amended and as further amended by the Supplemental Resolution adopted by the Corporation on May 6, 2003, as supplemented by the Series 2003A-1 and Series 2003A-2 Bond Resolution, and as from time to time amended or supplemented in accordance with the terms and provisions of the Resolutions.

“Revenue Account” means the special trust account so denominated established pursuant to the Resolutions.

“Revenues” means (i) all receipts in respect of payments, proceeds, charges and other cash income received by the Corporation, by the Servicer or by the Trustee for the account of the Corporation from or on account of any Loan, or as a result of the sale or alienation thereof (including scheduled, delinquent and advance payments of interest or principal on any Loan or other payment received by the Trustee, the Corporation or a Servicer with respect to any Loan, but excluding any amount retained by the Servicer of any Loan as compensation for services rendered in connection with the servicing of such Loan); (ii) all interest earned or gain realized from the investment of amounts in any Account (other than amounts credited or required to be deposited to the Operating Account, Earnings Account and the Rebate Account); and (iii) any amount received by the Trustee under any Swap or Swap Facility (other than an initial payment by the Swap Provider assigned by the Corporation to the Trustee for deposit to the credit of the Operating Account) including, without limitation, any Swap Receipts and Termination Receipts.

“SEC” means the Securities and Exchange Commission.

“Securities Depository” means DTC and its successors and assigns or if: (i) the then Securities Depository resigns from its functions as depository of the Obligations; or (ii) the Corporation discontinues use of the Securities Depository, any other securities depository which agrees to follow the procedures required to be followed by a securities depository in connection with the Obligations and which is selected by the Corporation with the consent of the Trustee and each applicable Obligation Facility Provider.

“Senior Obligations” means the Class of Obligations issued pursuant to the Resolutions in accordance with the requirements thereof and having a priority of claim as to payment from the Trust Estate that is equal to that of all other Senior Obligations and senior to that of all Subordinate Obligations (including Senior Subordinate Obligations); provided, that at any time at which no Obligations issued or originated as Senior Obligations remain Outstanding, Senior Obligations shall be deemed to mean the most senior Class of Obligations issued or originated as Subordinate Obligations (including Senior Subordinate Obligations) then Outstanding, except that in no event shall Subordinate Obligations (including Senior Subordinate Obligations) be deemed to be Senior Obligations for purposes of priority of claim as to payment under the Resolutions.

“Senior Subordinate Obligations” means the Class of Subordinate Obligations issued pursuant to the Resolutions in accordance with the requirements thereof and having a priority of claim as to payment from the Trust Estate that is: (i) subordinate to all Senior Obligations; (ii) equal to that of all other Senior Subordinate Obligations; and (iii) senior to that of all other Subordinate Obligations.

“Separately Secured Financing” means evidences of indebtedness or other financial instruments issued or entered into by the Corporation under a resolution, indenture of trust or other financing document establishing another and separate trust estate, which are described in the Resolutions.

“Series” means all of the Obligations authenticated and delivered on original issuance in any subsequent simultaneous transaction, pursuant to the same Series Resolution and designated as a Series in such Series Resolution regardless of variations in maturity, interest rate or other provisions, and any Obligations thereafter authenticated and delivered in lieu of or in substitution for (but not to refund) such Obligations as provided in the Resolutions.

“Series 2003A-1 and Series 2003A-2 Bond Resolution” means the Series 2003A-1 and 2003A-2 Bond Resolution adopted by the Corporation on May 6, 2003.

“Series Resolution” means any instrument supplemental to or amendatory of the Resolutions adopted by the Corporation in accordance with the provisions of the Resolutions.

“Servicer” means, with reference to any Series of Obligations, (i) the Corporation or any successor, subsidiary or other affiliated entity of the Corporation succeeding to such function; and (ii) such other entity as may be appointed by the Corporation in accordance with any Servicing Agreement.

“Servicing Agreement” means, with respect to any Series of Obligations, any agreement providing for the servicing of Loans financed through application of the proceeds of such Series.

“Student Loan” means an obligation representing advances of money to, or for the benefit of, a student evidenced by one or more promissory notes or otherwise evidenced in such manner as may be described by a Certificate of an Authorized Officer to the Trustee: (A) which are originated pursuant to the Higher Education Act: (i) the holder of which is eligible (in the case of loans originated pursuant to programs qualifying therefor) for special allowance payments and (in the case of loans originated pursuant to programs qualifying therefor) for interest subsidy payments as provided by the Higher Education Act; (ii) the payment of principal of and interest on which is guaranteed or insured by a Guaranty Agency and reinsured as to the principal amount thereof and interest thereon by the Secretary of Education in accordance with the requirements of the Higher Education Act, or insured as to principal amount and interest directly by the Secretary of Education; (iii) which are originated in accordance with Applicable Law; and (iv) which contain terms in accordance with those required by the Higher Education Act

and the applicable Guaranty Agency requirements; or (B) which are originated under such other program as may be described by a Certificate of an Authorized Officer to the Trustee accompanied by a Rating Affirmation and originated in accordance with Applicable Law.

“Subordinate Obligations” means any Class of Obligations issued pursuant to the Resolutions in accordance with the requirements thereof and having a claim as to payment from the Trust Estate that is equal to that of all other Subordinate Obligations of the same Class and subordinate to that of all Senior Obligations. Multiple Classes of Subordinate Obligations may be issued in accordance with the requirements of the Resolutions having different priorities of claim as to payment from the Trust Estate.

“Subseries” means: (i) such portion of the Obligations authenticated and delivered on original issuance as part of a single Series as may be so designated in the Series Resolution authorizing such Series regardless of variations in maturity, interest rate or other provisions; and (ii) any Obligations thereafter authenticated and delivered in lieu of or in substitution for (but not to refund) Obligations of such Subseries as provided in the Resolutions.

“Swap” means any financial arrangement: (i) that is entered into by the Corporation with an entity that is a Swap Provider at the time the arrangement is entered into; (ii) (a) which provides that the Corporation shall pay to such entity an amount based on the interest accruing at a fixed rate on the Notional Amount equal to all or part of the Outstanding principal amount of a Series of Obligations issued under the Resolutions, and that such entity shall pay to the order of the Corporation an amount based on the interest accruing on the Notional Amount at a variable rate of interest computed according to a formula set forth in such arrangement (which need not be the same as the actual rate of interest borne by such Series of Obligations) or that one (after adjustment for any cap, floor, collar or other financial arrangement referred to in (ii)(c) hereof, with respect thereto) shall pay to the other the net amount (Swap Payment or Swap Receipt) due under such arrangement; (b) which provides that the Corporation shall pay to such entity an amount based on the interest accruing on the Notional Amount equal to all or part of the Outstanding principal amount of a Series of Obligations issued under the Resolutions, at a variable rate of interest computed according to a formula set forth in such arrangement and that such entity shall pay to the order of the Corporation an amount based on the interest accruing at a fixed rate on the Notional Amount (which need not be the same as the actual rate of interest borne by such Series of Obligations) or that one (after adjustment for any cap, floor, collar or other financial arrangement referred to in (ii)(c) hereof, with respect thereto) shall pay to the other the net amount (Swap Payment or Swap Receipt) due under such arrangement; or (c) which is included as part of or covered by the financial transaction described in (ii)(a) or (ii)(b) above or is separately executed and which is a cap, floor or collar, forward rate, future rate, asset, swap or index, price or market linked transaction or agreement, other exchange or rate protection transaction agreement, other similar transaction (however designated) or any combination thereof or any option with respect thereto executed by the Corporation for the purpose of moderating interest rate fluctuations or otherwise pursuant to the Act; and (iii) which has been designated by a Certificate of an Authorized Officer to the Trustee and authenticated or otherwise registered by the Trustee under the Resolutions as a Swap with respect to a Series of Obligations. “Swap” shall also include any such financial arrangement described in clauses (ii) and (iii) above entered into by the Corporation with a Swap Provider as a replacement of a Swap that has been terminated and which has been so designated by a Certificate of an Authorized Officer to the Trustee with respect to a Series of Obligations.

“Swap Facility” means an insurance policy, surety bond, letter of credit or other credit enhancement with respect to a Swap or any similar facility entered into for the same or similar purposes and may include Investment Securities properly pledged to the Corporation under the Resolutions pursuant to the Swap Facility or by the Swap Provider, in each case satisfying or meeting the rating standards for investments of the Debt Service Reserve Account, which is delivered to the Trustee along with a Certificate of an Authorized Officer to which a Rating Affirmation is attached. Payments by the Corporation under a Swap Facility related to a Swap shall be deemed Swap Payments under the Resolutions and shall not be deemed Reimbursement Obligations and payments to the Corporation under a Swap Facility related to a Swap shall be deemed Swap Receipts. Payment by the Corporation under a Swap Facility applicable to any fees, expenses or similar other charges or obligations thereunder shall be a Cost of Issuance or a Program Expense.

“Swap Payment” means the net amount required to be paid in respect of interest by the Corporation under a Swap that is applicable to the interest rate exchange effected thereunder, but not (a) any fees, expenses or similar

other charges or obligations thereunder (which shall be either Program Expenses or Costs of Issuance) or (b) any Termination Payment or other payments by the Corporation on account of termination of the Swap (which shall be Other Obligations).

“Swap Provider” means a financial institution: (i) whose long term debt obligations are rated at least as high by at least two nationally recognized rating agencies as the greater of (a) the rating of the related Class of Bonds or Notes authorized by the applicable Series Resolution authorizing such Swap and (b) “Aa”; (ii) whose obligations under the Swap are fully covered by a Swap Facility and achieve the ratings described in (i); or (iii) whose obligations under the Swap are secured by a pledge of Defeasance Securities in amounts sufficient to achieve the ratings described in (i) hereof.

“Swap Receipt” means the net amount required to be paid to the Corporation under a Swap, but shall not include any Termination Receipt.

“Tax-Exempt” means, with respect to any Series or Subseries of Obligations, that interest received by Bondholders is not included in gross income for federal income tax purposes pursuant to Section 103 of the Code, as evidenced by a Counsel’s Opinion addressed to the Corporation.

“Termination Payment” means with respect to a Swap an amount required to be paid by the Corporation to the Swap Provider or related Swap Facility as a result of the termination of the Swap or pursuant to a Swap Facility; provided that any payments by the Corporation on account of termination of a Swap shall be deemed Other Obligations under the Resolutions.

“Termination Receipt” means with respect to a Swap an amount required to be paid to the Corporation by the Swap Provider or related Swap Facility as a result of the termination of the Swap.

“Trust Estate” means all property pledged under the Resolutions in trust for the benefit of the Owners of the Obligations pursuant to the granting clauses of the Resolutions or pursuant to any Series Resolution.

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## **Appendix C**

### **Summary of Certain Provisions of the Resolutions**

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## SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS

The Resolutions contain various covenants and security provisions, certain of which are summarized below and not otherwise deemed or discussed in this Official Statement. Reference should be made to the Resolutions for a full and complete statement of their provisions. The Resolutions may be modified by the provisions of Series Resolutions. The Corporation adopted a Supplemental Resolution on May 6, 2003 that will amend certain provisions of the General Resolution, upon its effective date, which is expected to be May 21, 2003, with respect to various matters. The summary below reflects such amendments.

**Contract with Holder.** The provisions of the Resolutions constitute a contract between the Corporation and the Owners of the Obligations, and the pledges and assignments made in the Resolutions and the provisions, covenants and agreements set forth therein are for the equal benefit, protection and security of the Owners of any and all of such Obligations, each of which, regardless of the time or times of its issue or maturity, shall be of equal rank without preference, priority or distinction over any other thereof, except as expressly provided in the Resolutions.

**Pledge Effected by the Resolutions.** To secure the payment of principal of and interest on the Obligations, there is pledged, subject to the provisions of the Resolutions permitting the application thereof, for or to the purposes and on the terms and conditions set forth in the Resolutions, the Trust Estate, including the following: (i) all moneys, including Obligation proceeds, held in any of the funds and accounts (other than the Rebate Account) established and held under the Resolutions or received by the Trustee for deposit in such funds and accounts (other than the Rebate Account); (ii) all Loans, the Corporation's right, title and interest in which is funded through the application of assets described in (i) above, along with all documentation thereof and all rights of the Corporation with respect thereto except as expressly provided in the Resolutions; (iii) all guarantee or insurance payments with respect to Loans and interest thereon described in (ii) above; (iv) any grant or contributions which may be received by the Corporation from any department, agency or instrumentality of the United States, or from any person; (v) all other Revenues; (vi) all rights of the Corporation with respect to any Origination Agreement or Servicing Agreement; (vii) all rights of the Corporation under any Swap or Swap Facility; and (viii) all direct and indirect proceeds, of any of the assets described in (i) through (vii) above. The pledge shall be valid and binding from and after the date of the Resolutions. In accordance with the statutory lien provisions of the Act, the Trust Estate so pledged shall immediately be subject to the lien of such pledge without any physical delivery or further act, and the lien of any such pledge shall be valid and binding as against all parties having claims of any kind in tort, contract or otherwise against the Corporation, irrespective of whether such parties have notice thereof.

**Nature of Security for Obligations.** (A) The Resolutions create an issue of Obligations of the Corporation and creates a continuing pledge and lien to secure the full and final payment of the principal of and interest on such Obligations. The Bonds, Notes, Reimbursement Obligations, Swap Payments and any other obligation of the Corporation arising under any Bond, Note, Obligation Facility or Swap shall be special and limited obligations of the Corporation, payable solely from the Trust Estate without recourse against other assets of the Corporation. The Bonds, Notes, Reimbursement Obligations, Swap Payments and any other obligation of the Corporation arising under any Bond, Note, Obligation Facility or Swap shall not be deemed to constitute a debt or liability of the Commonwealth or of any political subdivision thereof or a pledge of the faith and credit of the Commonwealth or of any such political subdivision other than the Corporation.

(B) The pledges and assignments made under the Resolutions and the provisions, covenants and agreements set forth in the Resolutions to be performed by or on behalf of the Corporation shall be for the equal benefit, protection and security of the Owners of any and all of such Obligations, each of which, regardless of the time or times of its issue or maturity, shall be of equal rank without preference, priority or distinction over any other thereof, except as expressly provided in the Resolutions.

(C) (i) Subject to the preceding paragraphs (A) and (B), all Bonds and Notes identified as Senior Obligations by the applicable Series Resolution authorizing their issuance shall have the same priority of claim as to payment under the Resolutions, which priority shall be senior to that of all Subordinate Obligations;

(ii) Subject to the preceding paragraphs (A) and (B), all Bonds and Notes identified as Senior Subordinate Obligations by the applicable Series Resolution authorizing their issuance shall have the same priority of claim as to payment under the Resolutions, which priority shall be subordinate to all Senior Obligations and senior to that of all Subordinate Obligations other than Senior Subordinate Obligations;

(iii) Subject to the preceding paragraphs (A) and (B), all Bonds and Notes identified as Subordinate Obligations, other than Senior Subordinate Obligations, having the same priority by the applicable Series Resolution authorizing their issuance shall have the same priority of claim as to payment under the Resolutions, which priority: (a) shall be subordinate: (I) to all Senior Obligations; (II) to all Senior Subordinate Obligations; (III) to all Subordinate Obligations expressly identified in such Series Resolution or, if not addressed in such Series Resolution, in a subsequent Series Resolution as senior to such Class; and (IV) to all Obligations having the same priority of claim as to payment as do Subordinate Obligations so expressly identified; and (b) shall be senior: (I) to all Subordinate Obligations expressly identified in such Series Resolution or, if not addressed in such Series Resolution, in a subsequent Series Resolution as subordinate to such Class; and (II) to all Obligations having the same priority of claim as to payment as do Subordinate Obligations so expressly identified;

(iv) Subject to the preceding paragraphs (A) and (B), Reimbursement Obligations and Swap Payments arising in connection with any Class of Bonds or Notes shall have the same priority of claim as to payment under the Resolutions as does the applicable Class of Bonds or Notes;

(v) Subject to the preceding paragraphs (A) and (B), Other Obligations shall have a priority of claim as to payment under the Resolutions which shall be either the same as or subordinate to the Reimbursement Obligations or Swap Payments in connection with which such Other Obligations arise as specified in the Series Resolution authorizing the applicable Class of Bonds or Notes; and

(vi) No Owner of Obligations shall have any claim to any amounts properly distributed from the Trust Estate from time to time pursuant to the Resolutions and the recipients of any amounts so distributed shall in no event be required to refund such properly distributed amounts.

**Establishment of Accounts.** (A) The Resolutions create the following special trust accounts to be held by the Trustee:

- (1) Loan Account;
- (2) Debt Service Reserve Account;
- (3) Revenue Account;
- (4) Operating Account;
- (5) Earnings Account; and
- (6) Rebate Account.

(B) The Trustee shall establish and create such separate funds within any of the Accounts established in subsection (A) of this Section as the Corporation may from time to time direct by delivery of a Certificate of an Authorized Officer or, subject to the written direction of the Corporation as the Trustee may deem advisable to facilitate the administration of the Trust Estate. Each such fund established within any Account shall be treated separately for record keeping and reporting purposes but all such funds established within any Account, other than the Rebate Account, shall constitute one undivided Account for all other purposes of the Resolutions except as the Corporation may direct by delivery of a Certificate of an Authorized Officer. Each such fund established within the

Rebate Account with respect to any Series or Subseries of Obligations shall be treated as the sole fund available in the Rebate Account with respect to such Series or Subseries while: (i) any amount remains credited to such fund; and (ii) any obligation of the Corporation with respect to amounts in the Earnings Account and the Rebate Account remain unpaid or unperformed with respect to such Series or Subseries; provided, that the Corporation may from time to time direct the Trustee to effect transfers between funds established in the Rebate Account by delivery of a Certificate of an Authorized Officer accompanied by a Counsel's Opinion to the effect that such transfer would not violate the provisions of the Resolutions relating to Tax-Exempt Obligations. The Trustee may establish and create such separate special trust accounts in addition to the Accounts established in subsection (A) of this Section as the Trustee may deem advisable to facilitate the transfer of cash, Investment Securities or Loans into or out of the Trust Estate or between Accounts established in subsection (A) of this Section. Each special trust account so established shall constitute a part of the Trust Estate and any asset deposited to any special trust account so established shall constitute an asset of the Trust Estate and, with respect to assets transferred from an Account established in subsection (A) of this Section to a special trust account so established, an asset of the Account from which such asset was so transferred for all purposes of the Resolutions.

(C) All moneys and securities deposited in the Accounts and held by the Trustee pursuant to the Resolutions shall be held in trust and applied only in accordance with the provisions of the Resolutions.

**Loan Account.** There shall be deposited to the credit of the Loan Account a portion of the proceeds of each Series other than any Series of Refunding Obligations. Amounts so credited which represent original proceeds of a Series of Obligations and which are deposited thereto for application to the financing and refinancing of Student Loans described in clause (A) of the definition thereof or pursuant to any program described in clause (B) of such definition shall be so applied prior to the application of amounts deposited to the credit of the Loan Account for such application from the proceeds of any subsequently issued Series of Obligations or from any other source.

Amounts in the Loan Account shall be expended only: (a) to finance and refinance Student Loans, including the payment of any origination fees, origination discounts, transfer fees and acquisition premiums, subject to any purchase price or origination cost limitations, as applicable, that may be imposed by the most recent Series Resolution addressing such limitations or to receipt by the Trustee of a Certificate of an Authorized Officer to which is attached a Rating Affirmation, and to pay Costs of Issuance; (b) to apply to the redemption of Obligations in accordance with the Resolutions; (c) to provide amounts for transfer to the Revenue Account in accordance with the Resolutions; and (d) to provide amounts for transfer to the Operating Account in accordance with the Resolutions. All Loans financed or refinanced by application of amounts in the Loan Account shall be credited to the Loan Account, notwithstanding that the notes or other evidence of such Loans may be held by a Servicer.

The Resolutions provide that the Corporation may at any time direct the Trustee in writing to apply amounts in the Loan Account to the redemption, purchase or retirement of any Obligations in accordance with their terms and the provisions thereof, but only if there is delivered to the Trustee, along with such written direction, a Certificate of an Authorized Officer stating that, in the judgment of the Corporation, such transfer or application would not materially and adversely affect the security pledged to the payment of any Obligations remaining Outstanding. The Resolutions further provide, with respect to the Senior Series 2003A Bonds, that all amounts credited to the Loan Account upon issuance of the Senior Series 2003A Bonds, as original proceeds of the Senior Series 2003A Bonds which have not been applied to finance Student Loans on or before July 1, 2005, or such later date as may be established by a Certificate of an Authorized Officer accompanied by a Rating Affirmation, shall be applied to the redemption of the Senior Series 2003A Bonds.

The Resolutions provide that, in the event that amounts available in the Revenue Account, along with all other amounts available for transfer to the Revenue Account from sources other than the Debt Service Reserve Account and the Loan Account, shall at any time be insufficient to fund payments therefrom in accordance with Paragraphs FIRST, SECOND, THIRD or FOURTH included under "SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS — Revenue Account" in this APPENDIX C, the Trustee shall transfer the amount necessary to fund such payment to the Revenue Account, but only to the extent of cash then credited to the Loan Account without liquidating Loans credited thereto.

The Resolutions provide that, in the event that amounts available in the Revenue Account, along with all other amounts available for transfer to the Revenue Account from sources other than the Loan Account, shall at any

time be insufficient to fund payments therefrom in accordance with Paragraphs FIRST, SECOND, THIRD or FOURTH included under “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTIONS — Revenue Account” in this APPENDIX C, the Trustee shall transfer the amount necessary to fund such payment to the Revenue Account and shall liquidate Loans to the extent necessary to effect such transfer.

The Resolutions provide that, subject to any provision contained in a Series Resolution limiting the payment of Program Expenses, in the event that the amounts available in the Operating Account, along with all other amounts available for transfer to the Operating Account from sources other than the Loan Account, shall at any time be insufficient to pay estimated Program Expenses then unpaid or becoming payable during the applicable period beginning on the next preceding Interest Payment Date, or during the applicable period beginning on the date of issuance, as estimated by the Corporation and as set forth in the Certificate of an Authorized Officer, the Corporation shall direct the Trustee to and the Trustee, upon receipt of such Certificate, shall transfer the amount set forth in such Certificate to the Operating Account.

The Series 2003A-1 and Series 2003A-2 Bond Resolution limits the annual amount expended from the Trust Estate to pay certain Program Expenses to the aggregate amount of (i) 1.45% of the principal balance of Loans credited to the Loan Account that are attributable to any Tax-Exempt Series of Bonds, and (ii) 1.30% of the principal balance of Loans credited to the Loan Account that are not attributable to any Tax-Exempt Series of Bonds or such other percentage as may be established by a Certificate of an Authorized Officer accompanied by a Rating Affirmation.

**Debt Service Reserve Account.** Except as may be set forth in any Series Resolution, in the event that amounts available in the Revenue Account are insufficient, subsequent to any transfer thereto from the Loan Account as set forth in the Resolutions, to fund certain payments therefrom, including the principal of, or the interest on, the Senior Obligations or the Subordinate Obligations, the Trustee shall transfer the amount necessary to fund such payment from the Debt Service Reserve Account to the Revenue Account.

In the event that amounts in the Debt Service Reserve Account shall at any time exceed the aggregate requirement therefor established by each applicable Series Resolution, taking into account all transfers and payments of principal to be effected on the date of calculation, such excess shall be transferred, upon the written direction of the Corporation, to the Revenue Account or the Loan Account or, in the absence of such direction, to the Revenue Account.

**Revenue Account.** Except as otherwise provided by a Series Resolution, all Revenues are to be deposited promptly with the Trustee in the Revenue Account. The Trustee is to apply, at the direction of the Corporation, all moneys then deposited therein as follows and in the following order of priority:

- FIRST:            On any Business Day, to apply to the payment to a borrower or to the federal government of amounts required pursuant to the Applicable Law with respect to rebates of amounts paid by borrowers, to origination fees and to insurance or to guarantee fees, as established by delivery of a Certificate of an Authorized Officer;
- SECOND:        With respect to any Tax-Exempt Series or Subseries of Obligations, on any Business Day, to transfer to the credit of the Rebate Account, to the extent of funds available, an amount sufficient, along with the other amounts: (i) credited thereto, subsequent to all transfers or credits thereto on the preceding Business Day; (ii) credited thereto on such Business Day as earnings upon the Rebate Account; or (iii) transferred thereto on such Business Day from the Earnings Account, to fund required payments from the Rebate Account on such date;
- THIRD:         With respect to any Tax-Exempt Series or Subseries of Obligations, on any Business Day, to apply in accordance with the requirements of the Arbitrage Certificate to assure compliance with the Resolutions;
- FOURTH:        On any Interest Payment Date, other date upon which principal of Obligations is payable or other date upon which a Reimbursement Obligation or Swap Payment is payable, and

subsequent to the foregoing applications, to transfer to the Paying Agent an amount sufficient to fund payments in the following order of priority: (i) all interest, Reimbursement Obligations in respect of interest and Swap Payments on Senior Obligations due on such date, and all principal and Reimbursement Obligations in respect of principal of Senior Obligations due on such date (other than pursuant to optional redemption), on a pro rata basis within such Class; (ii) to the credit of the Debt Service Reserve Account, the amount necessary to cause the balance therein to equal the aggregate requirement therefor established in each Series Resolution; and (iii) with respect to each successive Class of Subordinate Obligations having the next most senior priority as to payment hereunder, all interest, Reimbursement Obligations in respect of interest and Swap Payments due on such date and all principal and Reimbursement Obligations in respect of principal due on such date (other than pursuant to optional redemption), on a pro rata basis within such respective Class;

- FIFTH: On the last Business Day of each calendar quarter and subsequent to the foregoing applications, to transfer to the credit of the Operating Account, to the extent of amounts available, an amount sufficient, along with all other amounts available therefor, to pay Program Expenses then unpaid and payable or becoming payable during the next quarterly period;
- SIXTH: On any Interest Payment Date and subsequent to the foregoing applications, to transfer to the Paying Agent an amount sufficient to fund payment of any Carry-over Amount payable pursuant to any Series Resolution, with respect to each successive Class of Senior and Subordinate Obligations, in descending order of priority as to payment hereunder, on a pro rata basis within such respective Class;
- SEVENTH: On any date upon which Obligations are payable pursuant to redemption, and subsequent to the foregoing applications, to transfer to the Paying Agent an amount sufficient to fund payments in the following order of priority: (i) all principal and Reimbursement Obligations in respect of principal of Senior Obligations due on such date pursuant to optional redemption along with any associated premium, on a pro rata basis within such Class; and (ii) all principal and Reimbursement Obligations in respect of principal of each successive Class of Subordinate Obligations having the next most senior priority as to payment hereunder due on such date pursuant to optional redemption, along with any associated premium, on a pro rata basis within such respective Class;
- EIGHTH: On any Interest Payment Date and subsequent to the foregoing applications, if so directed by a Certificate of an Authorized Officer, to transfer to the Paying Agent the amount so certified for application to the redemption of Obligations as directed in such Certificate in accordance with their terms and the provisions of the Resolutions;
- NINTH: On any Interest Payment Date and subsequent to the foregoing applications, if: (i) so directed by a Certificate of an Authorized Officer stating the amount of Excess Coverage which would otherwise exist, after giving effect to all other transfers made or to be made pursuant to the Resolutions on such date; and (ii) a Cash Flow Projection shall have been delivered to each Rating Agency, with a copy to the Trustee, which Cash Flow Projection shall be prepared assuming such transfer, to transfer in accordance with a Certificate of an Authorized Officer, an amount not in excess of the amount of Excess Coverage so certified free and clear of the lien of the Resolutions; and
- TENTH: On any Interest Payment Date which occurs prior to the end of any applicable Recycling Period and subsequent to the foregoing applications, to transfer to the credit of the Loan Account an amount established by delivery of a Certificate of an Authorized Officer evidencing that the aggregate amount of funds credited to the Loan Account which the Corporation then projects that it might apply, if credited to the Loan Account to finance

Student Loans during the then current Fiscal Year, exceeds the amount credited to the Loan Account and available for such purpose by at least such amount.

**Operating Account.** Amounts on deposit in the Operating Account shall be used only to pay Program Expenses as due and may be released to the Corporation for such purpose on the last Business Day of any calendar month, or on such other monthly or less frequent schedule as may be requested by the Corporation from time to time in writing with respect to any Series of Obligations in an amount not exceeding the estimated amount of Program Expenses then unpaid or becoming payable during the next succeeding calendar month, as established by delivery of a Certificate of an Authorized Officer setting forth such amount; provided, that the portion of such amounts attributable to any Series to which an Obligation Facility applies shall be paid to the applicable Obligation Facility Provider upon the written direction of such applicable Obligation Facility Provider received by the Trustee during any period subsequent to an Event of Default and prior to an Obligation Facility Provider Default; and, further provided, that the aggregate amount so released or paid within any calendar quarter shall not exceed the assumption therefor reflected in the then current Cash Flow Projection.

**Earnings Account.** With respect to the Senior Series 2003A Bonds and any other Tax-Exempt Series or Subseries of Obligations, there shall be credited to the Earnings Account all amounts received in any Account, other than the Rebate Account, as interest earnings or net gain on disposition of investments, other than Loans, in excess of the Obligation Yield, but only if such deposit is required by the applicable Arbitrage Certificate.

With respect to the Senior Series 2003A Bonds and any other Tax-Exempt Series or Subseries of Obligations, but only if such deposit is required by the applicable Arbitrage Certificate, on the first Business Day following each computation period, amounts in the Earnings Account shall be deposited into the Rebate Account such that the amount held in the Rebate Account after such deposit is equal to the rebate amount calculated as of the last day of the computation period pursuant to written instructions from the Corporation. Following such transfers, any amounts on deposit in the Earnings Account shall be deposited to the Revenue Account.

**Rebate Account.** Upon receipt of written instructions from an Authorized Officer, amounts with respect to rebate liability which are transferred from the Earnings Account if applicable, or from the Revenue Account, to the Rebate Account shall be rebated to the United States at the times and in the amounts set forth in the Resolutions.

**Investment of Certain Funds.** Subject to the right of the Corporation to direct in writing the investment or deposit of funds in accordance with the Resolutions, moneys in any Account except as provided in the Resolutions shall be continuously invested and reinvested or deposited and redeposited by the Trustee in the highest yield Investment Securities, with a view toward maximizing yield (with proper preservation of principal) and minimizing the instances of uninvested funds.

Investment Securities purchased as an investment of moneys in any Account held by the Trustee under the Resolutions shall be deemed at all times to be a part of such Account, but with respect to any Tax-Exempt Series or Subseries of Obligations, the income or interest earned and gains realized in excess of losses suffered by an Account other than the Rebate Account due to the investment thereof shall be deposited in the Earnings Account, but only if such deposit is required by the applicable Arbitrage Certificate or, subject to compliance with certain requirements, shall be deposited in the Revenue Account or credited as Revenues to the Revenue Account from time to time and reinvested, in accordance with the Resolutions.

**Valuation of Investments.** In computing the amount in any Account, obligations other than Loans purchased as an investment of moneys therein shall be valued at amortized value, unless otherwise provided in the applicable Series Resolution provided, however, that Investment Securities credited to the Debt Service Reserve Account shall be valued at the then current market value as determined by the Trustee as of the last day of each month. Amortized value means par, if the obligation was purchased at par, or, when used with respect to an obligation purchased at a premium above or a discount below par, means the value as of any given time obtained by dividing the total premium or discount at which such obligation was purchased by the number of interest payments remaining on such obligation after such purchase and deducting the amount thus calculated for each interest payment date after such purchase from the purchase price in the case of an obligation purchased at a premium or adding the amount thus calculated for each interest payment date after such purchase to the purchase price in the case of an obligation purchased at a discount. Loans shall be valued at par plus: (i) accrued interest; and (ii) with

respect to Loans described in clause (A) of the definition thereof in the Resolutions, accrued but unpaid federal obligations, if any, other than interest, applicable to such Loans, in each case as evidenced by the Certificate of an Authorized Officer.

**Loan Program.** The Corporation shall, from time to time, with all practical dispatch and in a sound and economical manner consistent in all respects with the Resolutions and sound banking practices and principles: (i) do all such acts and things necessary to receive and collect Revenues sufficient to pay the expenses of the Loan Program; and (ii) diligently enforce and take all steps, actions and proceedings reasonably necessary in the judgment of the Corporation to protect its rights with respect to, to maintain any insurance on and to enforce all terms, covenants and conditions of Loans.

For so long as any Obligations are Outstanding, the Corporation shall administer the Loan Program in such manner as to ensure that the Loan Program and the Loans will benefit, to the optimum extent, from its contractual rights relative to all Loans.

The Corporation shall, either directly, or through its Servicers, diligently collect all principal and interest payments on all Loans held under the Resolutions, and all applicable interest subsidy payments, surety, insurance or guarantee claims and special allowance payments; subject, however, to the reserved rights of the Corporation: (i) to implement programs which have the effect of reducing Student Loan revenue received for purposes of reducing overall costs of administering such Student Loans or of benefiting the borrowers; and (ii) subsequent to delivery to the Trustee of a Certificate of an Authorized Officer to which is attached a Rating Affirmation and, if any Tax-Exempt Series or Subseries of Obligations is then Outstanding, a Counsel's Opinion to the effect that the capacity of the Corporation to comply with the Tax Covenants set forth in the Resolutions with respect to such Series or Subseries would not be materially reduced solely as a result thereof, to finance and refinance Student Loans which are affected by such programs by application of amounts in the Loan Account. The Corporation shall, or through its Servicers shall, cause the filing and assignment of such claims within the time prescribed by Applicable Law. The Corporation will remain, with respect to such Loans, in material compliance with all Applicable Law which applies to the Loan Program and to such Loans and will take no action to jeopardize the right to receive any federal payments with respect to the Loans described in clause (A) of the definition of Student Loans to which such payments may be applicable.

Except as otherwise provided in the Resolutions, the Corporation may at any time sell, assign, transfer or otherwise dispose of Loans credited to the Loan Account:

(i) provided, that the cumulative principal amount of Loans so disposed of, other than to trust estates securing Corporation obligations, since the most recent Series Resolution imposing or amending a limitation upon the aggregate principal amount of Loans which may be so disposed of does not exceed such limitation (such limitation is currently \$25,000,000) or that the Trustee has received a Certificate of an Authorized Officer describing such disposition to which is attached a Rating Affirmation, and that the aggregate price, in the form of cash or Student Loans, of the Loans so disposed will be at least equal to the aggregate principal amount of such Loans plus accrued interest, interest subsidy payments and special allowance payments thereon; and

(ii) at an aggregate price at least equal to the aggregate principal amount thereof (plus accrued borrower interest), when necessary to fund a transfer pursuant to the Resolutions.

Under all circumstances, the Corporation shall sell Loans if necessary to prevent the occurrence of an Event of Default.

**Power to Issue Obligations and Pledge Revenues, Funds and Other Property.** The Corporation is duly authorized under all applicable laws to authorize and issue the Obligations and to enter into, execute and deliver the Resolutions and to pledge the assets and revenues purported to be pledged thereby in the manner and to the extent therein provided. The assets and revenues so pledged are and will be free and clear of any pledge, lien, charge or encumbrance thereon, or with respect thereto prior to, or of equal rank with, the pledge created thereby, and all corporate or other action on the part of the Corporation to that end has been and will be duly and validly taken. The Obligations are and will be the valid and legally enforceable obligations of the Corporation in accordance with their

respective terms and the terms of the Resolutions. The provisions of the Resolutions are and will be a valid and legally enforceable obligation of the Corporation in accordance with its terms. The Corporation shall at all times, to the extent permitted by law, defend, preserve and protect the pledge of the Revenues and other assets and revenues, including rights therein pledged under the Resolutions, and all the rights of the Holders under the Resolutions against all claims and demands of all persons whomsoever.

**Further Assurance.** At any and all times the Corporation shall, so far as it may be authorized by law, pass, make, do, execute, acknowledge and deliver, all and every such further resolutions, acts, deeds, conveyances, assignments, transfers and assurances as may be necessary or desirable for the better assuring, conveying, granting, pledging, assigning and confirming all and singular the rights, Revenues and assets hereby pledged or assigned, or intended so to be, or which the Corporation may become bound to pledge or assign.

**Tax Covenants.** With respect to the Senior Series 2003A Bonds and any other Tax-Exempt Series or Subseries of Obligations, the Corporation shall at all times do and perform all acts and things necessary or desirable to assure that interest paid on the Obligations shall, for the purposes of federal income taxation, be excludable from the gross income of the recipients thereof and exempt from such taxation. The Corporation shall not permit at any time or times any of the proceeds of the Senior Series 2003A Bonds and any other Tax-Exempt Series or Subseries of Obligations or any other funds of the Corporation to be used directly or indirectly to acquire any securities or obligations, the acquisition of which would cause any of the Senior Series 2003A Bonds or any of such other Tax-Exempt Series or Subseries of Obligations to be an “arbitrage bond” as defined in the Code.

**Resolutions Effective Upon Filing with the Trustee.** For any one or more of the following purposes and at any time or from time to time, a Resolution of the Corporation may be adopted, which, upon the filing with the Trustee and each Obligation Facility Provider applicable to an affected Series of a copy thereof so identified by a Certificate of an Authorized Officer, shall be fully effective in accordance with its terms upon the fifteenth day subsequent to such filing, or with respect to any Resolution exclusively for the purpose described in paragraph (5) of this Section shall be fully effective as provided in such Resolution; provided, that the written consent of any affected Obligation Facility Provider to any such Resolution, other than a Resolution described in paragraph (5), (6) or (7) (which shall require no consent except such consent as may be required by a Resolution authorizing any Series of Obligations) has been received by the Trustee on or prior to such date, or else upon receipt of such consent:

- (1) to add to the Resolutions other covenants and agreements to be observed by the Corporation which are not contrary to or inconsistent with the Resolutions as theretofore in effect; or
- (2) to add to the Resolutions other limitations and restrictions to be observed by the Corporation which are not contrary to or inconsistent with the Resolutions as theretofore in effect; or
- (3) to surrender any right, power or privilege reserved to or conferred upon the Corporation by the terms of the Resolutions, but only if the surrender of such right, power or privilege is not contrary to or inconsistent with the covenants and agreements of the Corporation contained in the Resolutions; or
- (4) to confirm, as further assurance, any pledge under, and the subjection to any lien or pledge created or to be created by, the Resolutions, of the Revenues or of any other revenues or assets; or
- (5) to authorize the issuance of one or more Series of Obligations and to prescribe the terms and conditions upon which such Obligations may be issued; or
- (6) to modify any provision of the Resolutions if such modification is applicable only to Obligations to be issued subsequent to the effective date of such Series Resolution and if, in Counsel's Opinion, such modification does not materially affect any Outstanding Series; or
- (7) to implement any change in the corporate structure of the Corporation subsequent to the date hereof which results in the assignment of the duties of the Corporation hereunder to one or more successor, subsidiary or affiliated entities.



**Series Resolutions Effective Upon Consent of Trustee.** (A) For any one or more of the following purposes, a Series Resolution may be adopted, which, upon (i) the filing with the Trustee and each Obligation Facility Provider applicable to an affected Series of a copy thereof certified by a Authorized Officer, and (ii) the filing with the Trustee, each applicable Obligation Facility Provider and the Corporation of an instrument in writing made by the Trustee consenting thereto, shall be fully effective in accordance with its terms upon the fifteenth day subsequent to such filing; provided, that the written consent of each applicable Obligation Facility Provider to any such Series Resolution is received by the Trustee on or prior to such date, or else upon receipt of such consent:

- (1) to cure any ambiguity, supply any omission, or cure or correct any defect or inconsistent provision in the Resolutions; or
- (2) to insert such provisions clarifying matters or questions arising under the Resolutions as are necessary or desirable and are not contrary to or inconsistent with the Resolutions as theretofore in effect; or
- (3) to provide for additional duties of the Trustee in connection with the Loans; or
- (4) to provide for the orderly sale or remarketing of Obligations.

(B) Any such Series Resolution may also contain one or more of the purposes specified in the section entitled “Series Resolutions Effective Upon Filing With the Trustee” above, and in that event, the consent of the Trustee shall be required only to those provisions of such Series Resolution as shall contain one or more of the purposes set forth in subsection (A) above.

**Series Resolutions Effective Upon Consent of Holders.** A Series Resolution may be adopted subject to consent by Holders in accordance with and subject to the Resolutions and each Obligation Facility Provider. Any such Series Resolution shall become fully effective upon the filing with the Trustee of a copy thereof certified by an Authorized Officer and upon compliance with the Resolutions.

**Powers of Amendment.** Any modification of or amendment to the Resolutions may be made by a Series Resolution, but only, in the event such Series Resolution shall be pursuant to the Section entitled “Series Resolution Effective upon Consent of Holders”, with the written consent given as provided in the Resolutions (i) of the Owners of at least fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations which are Outstanding at the time such consent is given or (ii) in case less than all of the Most Senior Outstanding Obligations then Outstanding are affected by the modification or amendment, of the Owners of at least fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations so affected and Outstanding at the time such consent is given; provided, that consent of the applicable Obligation Facility Provider shall be deemed to establish consent of at least fifty-one percent (51%) of the Owners of a Series if such Obligation Facility Provider is providing an Obligation Facility with respect to all Obligations of such Series. If any such modification or amendment will not take effect so long as any Most Senior Outstanding Obligations of a specified maturity remain Outstanding, however, the consent of the Owners of such Most Senior Outstanding Obligations shall not be required and such Most Senior Outstanding Obligations shall not be deemed to be Outstanding for the purpose of any calculation of Most Senior Outstanding Obligations Outstanding under the Resolutions. No such modification or amendment shall permit a change in the terms of redemption or maturity of the principal of any Outstanding Obligation or of any installment of interest thereon or a reduction in the principal amount or redemption price thereof or in the rate of interest thereon without the consent of the Owner of such Obligation or shall reduce the percentages or otherwise affect the Classes of Obligations, the consent of the Owners of which is required to effect any such modification or amendment, or shall change or modify any of the rights or obligations of any Fiduciary without its written assent thereto. The Trustee may in its sole discretion determine whether or not in accordance with the foregoing powers of amendment Obligations of any particular maturity would be affected by any modification or amendment of the Resolutions and any such determination shall be binding and conclusive on the Corporation and all Owners of Obligations. No such modification or amendment shall change or modify any of the rights or obligations of any Fiduciary without the filing with the Trustee of the written assent thereto of such Fiduciary in addition to the consent of the Holders.

**Consent of Holders.** (A) A copy of any Series Resolution making a modification or amendment which is not permitted by the Resolutions (or brief summary thereof or reference thereto in form approved by the Trustee), together with a request for their consent thereto, shall be mailed by the Corporation to each applicable Obligation Facility Provider, prior to an Obligation Facility Provider Default, or to the Owner of each Most Senior Outstanding Obligation after an Obligation Facility Provider Default. Such Series Resolution shall not be effective unless (i) there shall have been filed with the Trustee (a) the written consents specified above in “Powers of Amendment” and (b) a Counsel’s Opinion stating that such Series Resolution has been duly and lawfully adopted by the Corporation in accordance with the provisions of the Resolutions, is authorized or permitted by the Resolutions and is valid and binding upon the Corporation, (ii) published notice shall have been given as hereinafter provided in the Resolutions and (iii) the written consent of each applicable Obligation Facility Provider has been received by the Trustee.

(B) Notice stating in substance that the Series Resolution has been consented to by the Owners of the required percentages of Most Senior Outstanding Obligations and will, subject to receipt of consent by each applicable Obligation Facility Provider, be effective as provided in the Resolutions, shall be given to Holders by the Corporation: (i) either by publication in not less than two newspapers or financial journals printed in the English language and customarily published (except in the case of legal holidays) at least once a day for at least five days in each calendar week, one of which is of general circulation in the City of Louisville, Kentucky and one of which is of general circulation in the Borough of Manhattan, City and State of New York or by distribution by electronic medium devoted to matters affecting the public market for obligations of Commonwealth and local governments and their instrumentalities and deposit with a municipal bond secondary market disclosure repository approved for such purpose by the federal Securities and Exchange Commission or the Municipal Securities Rulemaking Board; and (ii) by mailing such notice to the Holders (but failure to mail such notice shall not prevent such Series Resolution from becoming effective and binding as provided in this Section). Such Series Resolution making such amendment or modification shall be deemed conclusively binding upon the Corporation, the Fiduciaries, the Owners of all Obligations and each applicable Obligation Facility Provider upon its execution and delivery in accordance with the provisions of the Resolutions.

**Modifications by Unanimous Consent.** The terms and provisions of the Resolutions and the rights and obligations of the Corporation and of the Owners of the Obligations may be modified or amended in any respect upon the adoption and filing by the Corporation of a Series Resolution and the consent of each applicable Obligation Facility Provider and of Owners of all the Obligations then Outstanding, but no such modification or amendment shall change or modify any of the rights or obligations of any Fiduciary without the filing with the Trustee of the written assent thereto of such Fiduciary in addition to the consent of the Holders. No notice of any such modification or amendment to Holders shall be required.

**Events of Default.** Each of the following events is an “Event of Default” under the Resolutions:

(1) payment of the principal of or Redemption Price, if any, on any Most Senior Outstanding Obligation shall not be made when and as the same shall become due, whether at maturity or upon call for redemption or otherwise; or

(2) payment of any installment of interest on any Most Senior Outstanding Obligation shall not be made when and as the same shall become due; or

(3) the Corporation shall fail or refuse to comply with the other provisions of the Resolutions, or shall default in the performance or observance of any of the covenants, agreements or conditions on its part contained in the Resolutions or in the Obligations, and such failure, refusal or default shall continue for a period of thirty days after written notice thereof by the Trustee, each applicable Obligation Facility Provider or the Owners of not less than fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations Outstanding, except that if the Corporation is taking steps to cure the event and the event is curable within a reasonable period of time, such event shall not be an Event of Default; or

(4) the Corporation shall:

(a) admit in writing its inability to pay its debts generally as they become due; or

(b) consent to the appointment of a custodian (as that term is defined in the federal Bankruptcy Code) for, or assignment to a custodian of, the whole or any substantial part of the Corporation's property, or fail to cause to be stayed, set aside or vacated within one hundred and twenty (120) days from the date of entry thereof any order or decree entered by a court of competent jurisdiction ordering such appointment or assignment; or

(c) commence any proceeding or file a petition under the provisions of the federal Bankruptcy Code for liquidation, reorganization or adjustment of debts, or under any insolvency law or other statute or law providing for the modification or adjustment of the rights of creditors or fail to cause to be stayed, set aside or vacated within one hundred and twenty (120) days from the date of entry thereof any order or decree entered by a court of competent jurisdiction pursuant to an involuntary proceeding, whether under federal or state law, providing for liquidation or reorganization of the Corporation or modification or adjustment of the rights of creditors.

**Acceleration.** If any Event of Default specified in paragraphs (1) or (2) of the definition of "Event of Default" above shall have happened and be continuing, the Trustee may, and upon the written request of the Owners of not less than fifty-one percent (51%) in aggregate principal amount of Most Senior Outstanding Obligations Outstanding shall, by notice in writing delivered to the Corporation, declare the principal of and interest accrued on all Obligations then Outstanding immediately due and payable. At any time before such declaration, the Owners of twenty-five percent (25%) in principal amount of the Most Senior Outstanding Obligations Outstanding with, subject to the provisions of the Resolutions, the prior consent of each applicable Obligation Facility Provider, by written notice to the Corporation and the Trustee, may rescind and annul such direction and its consequences if:

(1) there has been paid to or deposited with the Trustee by or for the account of the Corporation, or provision satisfactory to the Trustee has been made for the payment of, a sum sufficient to pay:

(a) all overdue installments of interest on all Obligations;

(b) the principal of any Obligations which have become due otherwise than by such declaration of acceleration and interest thereon at the rate or rates borne by the Obligations;

(c) to the extent that payment of such interest is lawful, interest upon overdue installments of interest at the rate or rates borne by the Obligations; and

(d) all sums paid or advanced by the Trustee under the Resolutions, and the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel, and other Fiduciaries; and

(2) all Events of Default, other than the non-payment of the principal of and interest on Obligations which have become due solely by such declaration of acceleration, have been cured or waived as provided in the Resolutions.

No such rescission and annulment shall affect any subsequent default or impair any right consequent thereon.

**Other Remedies.** (A) Upon the happening and continuance of any Event of Default described in paragraphs (1) or (2) of the definition of "Event of Default" above, the Trustee shall immediately notify the Corporation, each applicable Obligation Facility Provider and each other Fiduciary of the existence of such Event of Default and shall proceed, or upon the happening and continuance of any Event of Default specified in paragraphs (3) or (4) of the definition of "Event of Default" above, the Corporation shall immediately notify the Trustee and each other Fiduciary and the Trustee may proceed and, upon the written request of the Owners of not less than fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations Outstanding or, prior to an Obligation Facility Provider Default of each applicable Obligation Facility Provider, shall proceed, in its own name, to protect and enforce the rights of the Holders and each applicable Obligation Facility Provider by such of the following remedies, as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce such rights:

(1) by mandamus or other suit, action or proceeding at law or in equity, to enforce all rights of the Holders and each applicable Obligation Facility Provider, including the right to require the Corporation to receive and collect Revenues adequate to carry out the covenants and agreements as to, and the assignment of, the Loans and to require the Corporation to carry out any other covenants or agreements with Holders and to perform its duties as prescribed by law;

(2) by bringing suit upon the Obligations;

(3) by action or suit in equity, to require the Corporation to account as if it were the trustee of an express trust for the Owners of the Obligations and each applicable Obligation Facility Provider;

(4) by action or suit in equity to enjoin any acts or things which may be unlawful or in violation of the rights of the Owners of the Obligations and each applicable Obligation Facility Provider;

(5) by declaring all Obligations due and payable, (but only with the written consent of all Owners of Most Senior Outstanding Obligations, if such Event of Default is the result of nonpayment of the principal of or interest on Subordinate Obligations, and only with the written consent of all Owners of Obligations, if such Event of Default is not the result of nonpayment of the principal of or interest on Obligations) and if all defaults shall be cured, then, with the written consent of the Owners of not less than fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations Outstanding and each applicable Obligation Facility Provider, by annulling such declaration and its consequences; or

(6) with, prior to an Obligation Facility Provider Default, the prior written consent of each applicable Obligation Facility Provider in the event that all Obligations are declared due and payable, by selling Loans credited to the Loan Account and Investment Securities.

(B) Except upon the occurrence and during the continuance of an Event of Default, the Corporation expressly reserves and retains the privilege to receive and, subject to the terms and provisions of the Resolutions, to keep or dispose of, claim, bring suit upon or to otherwise exercise, enforce or realize upon its rights and interest in and to the Loans and the proceeds and collections therefrom, and neither the Trustee, nor any applicable Obligation Facility Provider, nor any Holder shall in any manner be or be deemed to be an indispensable party to the exercise of any such privilege, claim or suit.

**Priority of Payments After Default.** In the event that upon the happening and continuance of any Event of Default the funds held by the Trustee and Paying Agents shall be insufficient for the payment of principal of or Redemption Price and interest then due on the Obligations, such funds (other than funds held for the payment of principal or premium of or interest on particular Obligations which have theretofore become due at maturity or redemption allocable to each Series affected), and any other amounts received or collected by the Trustee acting pursuant to the Resolutions after making provision for the payment of any expenses necessary in the opinion of the Trustee to protect the interest of the Owners of the Obligations and for the payment of the charges and expenses and liabilities incurred and advances made by the Trustee or any Paying Agents in the performance of their respective duties under the Resolutions, shall be applied to the extent allocable to each affected Series of Obligations as follows:

(1) Unless the principal of all of the Obligations shall have become or have been declared due and payable:

FIRST: To the payment to the persons entitled thereto of all installments of interest, Reimbursement Obligations in respect of interest and Swap Payments on Most Senior Outstanding Obligations then due in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full any installment, then to the payment thereof ratably, according to the amounts due on such installment, to the persons entitled thereto, without any discrimination or preference;

SECOND: To the payment to the persons entitled thereto of the unpaid principal and Reimbursement Obligations in respect of principal of Most Senior Outstanding Obligations, along with any

associated premium, which shall have become due and if the amounts available shall not be sufficient to pay in full all the Most Senior Outstanding Obligations due, then to the payment thereof ratably, according to the amounts of principal or Redemption Price due on such date, to the persons entitled thereto, without any discrimination or preference;

THIRD: With respect to each successive Class of Subordinate Obligations having the next most senior priority as to payment: (A) to the payment to the persons entitled thereto of all installments of interest, Reimbursement Obligations in respect of interest and Swap Payments on Obligations of such Class then due in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full any installment, then to the payment thereof ratably, according to the amounts due on such installments, to the persons entitled thereto, without any discrimination or preference; and (B) to the payment to the persons entitled thereto of the unpaid principal and Reimbursement Obligations in respect of principal of any Obligations of such Class which shall have become due, along with any associated premium, and, if the amounts available shall not be sufficient to pay in full all the Obligations of such Class due, then to the payment thereof ratably, according to the amounts of principal, along with any associated premium, due on such date, to the persons entitled thereto, without any discrimination or preference; and

FOURTH: To be held for the payment to the persons entitled thereto as the same shall become due, of the principal or Redemption Price of and interest on the Obligations which may thereafter become due and if the amounts available shall not be sufficient to pay in full all the Obligations due on any date, together with such interest, payment shall be made ratably according to the amount of principal and interest due on such date to the persons entitled thereto, without any discrimination or preference.

(2) If the principal of all of the Obligations shall have become or have been declared due and payable:

FIRST: to the payment of the principal and interest then due and unpaid upon the Most Senior Outstanding Obligations without preference of priority of principal over interest or of interest over principal, or of any installment of interest over any other installment of interest, or of any Most Senior Outstanding Obligation over any other Most Senior Outstanding Obligation, ratably, according to the amounts due respectively for principal and interest, to the persons entitled thereto without any discrimination or preference; and

SECOND: With respect to each successive Class of Subordinated Obligations having the next most senior priority as to payment, to the payment of the principal and interest then due and unpaid upon the Obligations of such Class without preference of priority of principal over interest or of interest over principal, or of any installment of interest over any other installment of interest, of or any Obligation of such Class over any other Obligation of such Class, ratably, according to the amounts due respectively for principal and interest, to the persons entitled thereto without any discrimination or preference.

**Termination of Proceedings.** In case any proceedings taken by the Trustee on account of any Event of Default shall have been discontinued or abandoned for any reason, then in every such case the Corporation, each applicable Obligation Facility Provider, the Trustee and the Holders shall be restored to their former positions and rights, respectively, and all rights, remedies, powers and duties of the Trustee shall continue as though no such proceedings had been taken.

**Direction of Proceedings by Holders or each applicable Obligation Facility Provider.** The Owners of a majority in aggregate principal amount of Most Senior Outstanding Obligations then Outstanding or, prior to an Obligation Facility Provider Default, each applicable Obligation Facility Provider, shall have the right, at any time, by an instrument or instruments in writing executed and delivered to the Trustee, to direct the method and place of conducting all proceedings to be taken in connection with the enforcement of the terms and conditions of the Resolutions, provided that: (a) such direction shall not be otherwise than in accordance with the provisions of law and of the Resolutions; (b) the Trustee shall not determine that the action so directed would be unjustly prejudicial to the Owners of Obligations not taking part in such direction; (c) the Trustee may take any other action deemed proper by the Trustee which is not inconsistent with such direction; and (d) the Trustee may initiate proceedings in Kentucky state court or in federal court located in Kentucky.

**Limitation on Rights of Holders.** (A) No Owner of any Obligation other than a Most Senior Outstanding Obligation shall have any right to institute any suit, action, mandamus or other proceeding in equity or at law hereunder, or for the protection or enforcement of any right under the Resolutions and no Owner of a Most Senior Outstanding Obligation shall have any such right unless such Owner shall have given to the Trustee written notice of the Event of Default or breach of duty on account of which such suit, action or proceeding is to be taken, and unless the Owners of not less than fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations then Outstanding shall have made written request of the Trustee after the right to exercise such powers or right of action, as the case may be, shall have occurred, and shall have afforded the Trustee a reasonable opportunity either to proceed to exercise the powers herein granted or granted under the law or to institute such action, suit or proceeding in its name and unless, also, there shall have been offered to the Trustee reasonable security and indemnity satisfactory to it against the costs, expenses and liabilities to be incurred therein or thereby, and the Trustee shall have refused or neglected to comply with such request within a reasonable time; and such notification request and offer of indemnity are hereby declared in every such case, at the option of the Trustee, to be conditions precedent to the execution of the powers under the Resolutions or for any other remedy under the Resolutions or by law. It is understood and intended that no one or more Owners of the Obligations secured by the Resolutions shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Resolutions, or to enforce any right under the Resolutions or under law with respect to the Obligations or the Resolutions, except in the manner provided by the Resolutions, and that all proceedings at law or in equity shall be instituted, had and maintained in the manner provided under the Resolutions and for the benefit of all Owners of the Outstanding Obligations. Nothing contained in the Article of the Resolutions entitled "Defaults and Remedies" shall affect or impair the right of any Holder to enforce the payment of the principal or purchase price of and interest on his Obligations, or the obligation of the Corporation to pay the principal or purchase price of and interest on each Obligation issued under the Resolutions to the Owner thereof at the time and place in said Obligation, if any, expressed.

(B) Anything to the contrary notwithstanding contained in this Section, or any other provision of the Resolutions, each Owner of any Obligation by his acceptance thereof shall be deemed to have agreed that any court in its discretion may require, in any suit for the enforcement of any right or remedy under the Resolutions or any Series Resolution, or in any suit against the Trustee for any action taken or omitted by it as Trustee, the filing by any party litigant in such suit of an undertaking to pay the reasonable costs of such suit, and that such court may in its discretion assess reasonable costs, including reasonable pre-trial, trial and appellate attorneys' fees, against any party litigant in any such suit, having due regard to the merits and good faith of the claims or defenses made by such party litigant; but the provisions of this paragraph shall not apply to any suit instituted by the Trustee, to any suit instituted by any Holder, or group of Holders, holding at least fifty-one percent (51%) in principal amount of the Most Senior Outstanding Obligations Outstanding, or to any suit instituted by any Holder of Most Senior Outstanding Obligations for the enforcement of the payment of any Most Senior Outstanding Obligation on or after the respective due date thereof expressed in such Obligation.

**Appointment of Successor Trustee.** (A) In case at any time the Trustee shall resign or shall be removed or shall become incapable of acting, or shall be adjudged a bankrupt or insolvent, or if a receiver, liquidator or conservator of the Trustee, or of its property, shall be appointed, or if any public officer shall take charge or control of the Trustee, or of its property or affairs, the Corporation covenants and agrees that it will thereupon appoint a successor Trustee.

(B) If in a proper case no appointment of a successor Trustee shall be made within sixty (60) days after the Trustee shall have given to the Corporation written notice of its resignation as Trustee, or after a vacancy in the office of the Trustee shall have occurred by reason of its inability to act, each applicable Obligation Facility Provider may appoint a successor Trustee or any of the Trustee, the Owner of any Obligation or each applicable Obligation Facility Provider may apply to any court of competent jurisdiction to appoint a successor Trustee.

(C) Any Trustee appointed under the provisions of the Resolutions shall be a corporation organized under the laws of the United States or of any state which is authorized to exercise trust powers and is subject to supervision or examination by federal or state authorities, having a capital, surplus and undivided profits aggregating at least \$75,000,000 and whose long-term obligations are rated not less favorable than "Baa" by each Rating Agency maintaining a rating with respect to any Outstanding Senior Series 2003A Bonds, if there be such a trust company or

bank willing and able to accept the office on reasonable and customary terms and authorized by law to perform all the duties imposed upon it by the Resolutions and shall be an Eligible Lender.

**Defeasance.** (A) If the Corporation shall pay or cause to be paid to the Owners of the Obligations, or of the Obligations of any Series or any Subseries, or of any maturity within a Series or Subseries, the principal and interest to become due thereon, at the times and in the manner stipulated therein and in the Resolutions, and all obligations of the Corporation thereunder with respect to the Obligations or to the Obligations of such Series or Subseries, or to any maturity within a Series or Subseries, as applicable, with respect to the fees and expenses of or reimbursement of each applicable Obligation Facility Provider, with respect to the fees and expenses of each Fiduciary and with respect to certain requirements applicable to the Senior Series 2003A Bonds and any other Tax-Exempt Obligations, have been paid or otherwise performed or the payment or performance thereof has otherwise been provided for to the satisfaction of the Trustee and each applicable Obligation Facility Provider, then the pledge of any Revenues and other moneys, securities, funds and property constituting a part of the Trust Estate and all other rights granted hereby shall be discharged and satisfied with respect to the Obligations or to the Obligations of such Series or Subseries, or to any such maturity, as applicable. In such event, the Trustee shall, upon the written request of the Corporation, execute and deliver to the Corporation all such instruments as may be desirable to evidence such discharge and satisfaction and the Fiduciaries shall pay over or deliver to the Corporation all moneys or securities held by them pursuant to the Resolutions which are not required for the payment of Obligations not theretofore surrendered for such payment. If the Corporation shall pay or cause to be paid, or there shall otherwise be paid, to the Owners of all Outstanding Obligations, or of the Obligations of any Series or Subseries, or of any maturity within a Series or Subseries, the principal and interest due or to become due thereon, at the times and in the manner stipulated therein and in the Resolutions, such Obligations shall cease to be entitled to any lien, benefit or security hereunder and all covenants, agreements and obligations of the Corporation to the Owners of such Obligations shall thereupon cease, terminate and become void and be discharged and satisfied.

(B) Obligations or interest installments for the payment of which moneys shall have been set aside and shall be held in trust by the Fiduciaries (through deposit by the Corporation of funds for such payment or otherwise) shall, at the maturity thereof, be deemed to have been paid within the meaning and with the effect expressed in subsection (A) of this Section. All Obligations shall, prior to the maturity or Redemption Date thereof, be deemed to have been paid within the meaning and with the effect expressed in subsection (A) of this Section if (i) in case any of said Obligations are to be redeemed on any date prior to their maturity, the Corporation shall have given to the Trustee in form satisfactory to it irrevocable written instructions to give notice as provided in the Resolutions of redemption on said date of such Obligations, (ii) there shall have been deposited with the Trustee either moneys or Defeasance Securities the principal of and the interest on which when due will provide moneys which, together with the moneys, if any, deposited with the Trustee at the same time, shall be sufficient to pay when due the principal or Redemption Price, if any, of and interest due and to become due on said Obligations on and prior to the Redemption Date or maturity date thereof, as the case may be, and (iii) in the event said Obligations are not by their terms subject to redemption within the next succeeding sixty days, the Corporation shall have given the Trustee in form satisfactory to it irrevocable written instructions to give notice to the Owners of such Obligations that the deposit required by (ii) above has been made with the Trustee and that said Obligations are deemed to have been paid in accordance with this Section and stating such maturity or Redemption Date upon which moneys are to be available for the payment of the principal or Redemption Price, if any, on said Obligations. Neither Defeasance Securities or moneys deposited with the Trustee pursuant to this Section nor principal or interest payments on any such Defeasance Securities shall be withdrawn or used for any purpose other than, and shall be held in trust for, the payment of the principal of or Redemption Price, if any, and interest on said Obligations; but any cash received from such principal or interest payments on such Defeasance Securities deposited with the Trustee, if not then needed for such purpose, shall, to the extent practicable, be reinvested in Defeasance Securities maturing at times and in amounts sufficient to pay when due the principal or Redemption Price, if any, and interest to become due on said Obligations on and prior to such maturity date thereof, as the case may be, and interest earned from such reinvestments shall be paid over to the Corporation, as received by the Trustee, free and clear of any trust, lien or pledge.

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**Appendix D**  
**Audited Financial Statements of**  
**the Corporation**

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# **KENTUCKY HIGHER EDUCATION STUDENT LOAN CORPORATION**

**Report on Audits of Financial Statements**

**for the year ended June 30, 2002**

## **C O N T E N T S**

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## Report of Independent Accountants

Board of Directors  
Kentucky Higher Education Student Loan Corporation  
Louisville, Kentucky

In our opinion, the financial statements of the Kentucky Higher Education Student Loan Corporation (the "Corporation"), a component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2002, as listed in the table of contents present fairly, in all material respects, the financial position of the Corporation as of June 30, 2002, and its changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these financial statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 2, the Corporation adopted the provisions of Governmental Accounting Standards Board Statement No. 34, "Basic Financial Statements -- Management Discussion and Analysis --for State and Local Governments" for the year ended June 30, 2002.

Management's Discussion and Analysis as set forth on pages 3 to 6 is not a required part of the basic financial statement but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated September 27, 2002 on our consideration of the Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

*PricewaterhouseCoopers LLP*

September 27, 2002

## **Kentucky Higher Education Student Loan Corporation Management's Discussion and Analysis**

The Kentucky Higher Education Student Loan Corporation (Corporation) is an independent *de jure* municipal corporation established by the Kentucky General Assembly in 1978 to provide a loan finance program for post-secondary students in the Commonwealth of Kentucky. The Corporation functions as a lender of student loans, making loans to parent and students directly; a servicer of student loans; and a secondary market for the purchase of student loans from other lenders. The Corporation funds the origination or acquisition of these student loans by periodically issuing bonds and notes under various debt agreements, including its two general bond resolutions. The Corporation also services education loans and collects defaulted education loans. The Corporation's services and loans are marketed under the registered service mark "The Student Loan People<sup>SM</sup>".

This section of the Corporation's annual financial report presents a discussion and analysis of the Corporation's financial performance for the fiscal year ended June 30, 2002. Please read it in conjunction with the Corporation's financial statements and the notes to the financial statements, which follow this section.

### **FINANCIAL HIGHLIGHTS AS OF JUNE 30, 2002:**

- The Corporation's total assets at year end were approximately \$900 million, which is an increase of approximately \$94,555,000 or 12% over the prior year.
- The Corporation's net student loans at year end were approximately \$716 million, which is an increase of approximately \$82 million or 13% over the prior year.
- The Corporation's total revenue for the fiscal year ended June 30, 2002 was approximately \$56 million, which is a decrease of approximately \$9 million or 14% from the prior fiscal year end.
- The Corporation's interest expense for the fiscal year ended June 30, 2002 was approximately \$23 million, which is a decrease of approximately \$15 million or 39% from the prior fiscal year end.
- The Corporation's total other operating expenses for the fiscal year were approximately \$21 million which is a decrease of approximately \$290,000 or 1% from the prior fiscal year end.
- The Corporation's change in net assets after operating transfers for the fiscal year ended June 30, 2002 was approximately \$10 million, which is an increase of approximately \$6 million or over double that of the prior fiscal year.

### **OVERVIEW OF THE FINANCIAL STATEMENTS:**

The Corporation's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied on an accrual basis. Under the accrual basis of GAAP, revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred. These basic financial statements are separated into funds. Certain provisions of each general bond resolution and the line of credit agreement (the three Education Finance Funds) require segregation of assets and restrictions on the use of certain funds. These requirements, as well as certain governmental accounting pronouncements, require this financial statement presentation.

# Kentucky Higher Education Student Loan Corporation Management's Discussion and Analysis

The three basic financial statements presented within the financial statements are:

## Balance Sheet

This statement presents information regarding the Corporation's assets, liabilities and net assets. Net assets represent the total amount of assets less the total liabilities. The balance sheet classifies assets, liabilities and classifies net assets as current, noncurrent, restricted and unrestricted according to restrictions in each general bond resolution.

## Statement of Revenues, Expenses and Change in Net Assets

This statement presents the Corporation's interest income, cost of funds, operating expenses and changes in net assets for the fiscal year.

## Statement of Cash Flows

The Corporation's statement of cash flows is presented using the direct method of reporting, which reflects cash flows from operating, investing, non-capital and capital financing activities.

## FINANCIAL ANALYSIS OF THE CORPORATION

The Corporation's total net assets at June 30, 2002 were approximately \$78.6 million, which is increase of approximately \$9.7 million or 14% over June 30, 2001. Components of the Corporation's balance sheet as of June 30, 2002 and 2001 were as follows:

**Kentucky Higher Education Student Loan Corporation**  
**Balance Sheet Data**  
*June 30, 2002 and 2001*

<b>Net Asset Information</b>	<b>2002</b>	<b>2001</b>	<b>Inc/(Decr)</b>	<b>%</b>
Loans	\$ 716,068,985	\$ 634,544,436	\$ 81,524,549	13%
Capital Assets	1,510,176	1,215,084	295,092	24%
Other Assets	181,870,363	169,134,931	12,735,432	8%
<b>Total Assets</b>	<b>\$ 899,449,524</b>	<b>\$ 804,894,451</b>	<b>\$ 94,555,073</b>	<b>12%</b>
<b>Liabilities and Net Assets</b>				
Short and Long-term debt	\$ 788,770,000	\$ 708,335,000	\$ 80,435,000	11%
Other liabilities	32,079,637	27,608,559	4,471,078	16%
<b>Total Liabilities</b>	<b>820,849,637</b>	<b>735,943,559</b>	<b>84,906,078</b>	<b>12%</b>
<b>Net Assets</b>				
Invested in Capital Assets	1,510,176	1,215,084	295,092	24%
Restricted	64,519,506	54,896,198	9,623,308	18%
Unrestricted	12,570,205	12,839,610	(269,405)	-2%
<b>Total Net Assets</b>	<b>78,599,887</b>	<b>68,950,892</b>	<b>9,648,995</b>	<b>14%</b>
<b>Total Liabilities and Net Assets</b>	<b>\$ 899,449,524</b>	<b>\$ 804,894,451</b>	<b>\$ 94,555,073</b>	<b>12%</b>

The increase noted above in the Corporation's total assets is the continuation of a trend of growth in prior years. Total assets grew from approximately \$805 million at June 30, 2001 to approximately \$900 million at June 30, 2002. Net loans outstanding totaled \$716 million at June 30, 2002, an \$82 million increase over June 30, 2001. This



## Kentucky Higher Education Student Loan Corporation Management's Discussion and Analysis

increase included \$179 million in loan acquisitions (both originations and purchases) offset by incoming payments on the loans. Other assets increased by \$12.7 million as a result of higher investment volume due to reduced debt service expense. During fiscal year 2002, the Corporation issued the Series 2001 A-1, A-2 and B bonds in the form of auction rate securities totaling \$150 million which was offset by approximately \$70 million in bond maturities and repayments on the line of credit. This increase was the largest component of the Corporation's increase in its total liabilities. Other liabilities increased \$4.5 million as a result of an increase in the allowance for arbitrage liabilities due to the increase in the excess yield on the loan portfolio.

The Corporation's change in net assets for the year ended June 30, 2002 was \$10 million, which is an increase of approximately \$6 million over the change in net assets for the year ended June 30, 2001. This amount is over double the prior year due to lower interest rates resulting in decreased interest on debt and a lower provision for arbitrage liabilities expense. Components of the Corporation's statement of revenues, expenses and change in net assets as of June 30, 2002 and 2001 were as follows:

**Kentucky Higher Education Student Loan Corporation  
Revenues, Expenses, and Changes in Net Assets Data**  
*Years ended June 30, 2002 and 2001*

**Activity Information:**

	2002	2001	Inc/(Decr)	%
<b>Revenues:</b>				
Loan Interest Income	\$ 47,738,650	\$ 51,631,802	\$ (3,893,152)	-8%
Investment Interest Income	4,853,260	10,466,255	(5,612,995)	-54%
Total Interest Income	52,591,910	62,098,057	(9,506,147)	-15%
Fee Income	3,777,722	3,143,341	634,381	20%
<b>Total Revenues</b>	<b>56,369,632</b>	<b>65,241,398</b>	<b>(8,871,766)</b>	<b>-14%</b>
<b>Expenses:</b>				
Interest Expense on Debt	22,626,945	37,324,921	(14,697,976)	-39%
Provision for Arbitrage Liabilities	4,810,982	6,832,323	(2,021,341)	-30%
Other Operating Expenses:				
Financing and Origination Fees	3,572,160	2,869,526	702,634	24%
Federal Consolidation Fees	1,307,673	1,096,754	210,919	19%
Personnel and Professional Services	5,964,854	5,172,507	792,347	15%
Technical Services	966,062	1,311,815	(345,753)	-26%
General Administration	4,471,961	4,100,985	370,976	9%
Total Other Operating Expenses	16,282,710	14,551,587	1,731,123	12%
<b>Total Expenses</b>	<b>43,720,637</b>	<b>58,708,831</b>	<b>(14,988,194)</b>	<b>-26%</b>
<b>Change in Net Assets before Operating Transfers</b>	<b>12,648,995</b>	<b>6,532,567</b>	<b>6,116,428</b>	<b>94%</b>
<b>Transfer to Other Funds:</b>				
Transfer to the Authority	(3,000,000)	(3,000,000)	-	-
<b>Change in Net Assets</b>	<b>\$ 9,648,995</b>	<b>\$ 3,532,567</b>	<b>\$ 6,116,428</b>	<b>173%</b>

Interest Income, which includes interest on loans and investments, decreased by 15% due to the declining interest rates in FY 2002. The average yield from interest on loans was 6.32% versus 8.09% in FY 2001. Likewise, investment yields declined from 6.03% in FY 2002 to 2.54% in FY 2001. Fee income increased due to the completion of a portfolio conversion from Access Group Inc., a large client for whom the Corporation

## **Kentucky Higher Education Student Loan Corporation Management's Discussion and Analysis**

performs third-party servicing activities. Interest on debt decreased by 39% due to declining interest rates on the variable rate bonds outstanding from an average of 5.32% in FY 2001 to 2.79% in FY 2002. The expense related to the provision for arbitrage liabilities decreased approximately \$2 million due to a decline in the absolute dollar volume increase and yield spread increase that occurred between fiscal 2001 and 2002.

Other operating expenses increased 12% due to costs related to the growing loan portfolio as the Corporation adds loan volume.

### **CONDITIONS AFFECTING FINANCIAL POSITION:**

At June 30, 2002, the Corporation was servicing and committed to purchase student loans from other lenders with a principal balance of approximately \$91 million. The total portfolio of student loans that the Corporation owns or services for other lenders was approximately \$2.9 billion at June 30, 2002. This is an increase of approximately \$1.5 billion or over double that as of June 30, 2001.

The Corporation continues to experience significant growth in all aspects of its operations and the Corporation's fiscal year 2003 budget reflects continued growth. Efforts to increase the Corporation's lending market share in the Commonwealth and the continued high rate of growth in the client servicing portfolio is expected to promote the sustained growth pattern for the Corporation throughout the coming fiscal year. The Corporation has added additional staff to perform the additional work associated with this significant growth and its anticipated expenses for fiscal year 2003 reflect the additional costs to be incurred as a result of the additional student loan volume.

Lower market interest rates at June 30, 2002 will result in lower student loan interest rates (that reset every July 1) on outstanding student loans in for fiscal year 2003, which will result in a reduction in the average yield for the total student loan portfolio.

Available and affordable funds from debt financings enable the Corporation to meet its lending demand for loans originated and purchased. Historically, the Corporation has issued primarily tax-exempt debt. However, since 1997 the Corporation has had to supplement its funding needs with taxable debt at a higher interest cost. Annually, the Corporation receives an allocation from the Commonwealth's Private Activity Bond Allocation committee which authorizes the amount of tax-exempt debt that the Corporation can issue. In July of 2002 the Corporation was allocated an additional \$27.5 million in authority to issue tax-exempt debt. The Corporation will utilize this additional allocation in fiscal year 2003 by issuing additional tax-exempt bonds. In addition to funds provided by the debt issuances, the Corporation also has a \$100 million line of credit with Bank of America for loan acquisitions. This line of credit provides additional liquidity in the event that loan demand exceeds the available funds from debt issuances. The Corporation has secured this line of credit through December 31, 2003 and expects to renew or replace this funding source to ensure available funds throughout fiscal year 2004. The Corporation and its trustee monitor the maturities of all debt instruments and the appropriate levels in the debt service and debt service reserve accounts. \$30.5 million in bonds will mature during the upcoming fiscal year and the Corporation expects its student loan payment stream to provide adequate funds to pay off these maturities.

**Kentucky Higher Education Student Loan Corporation**  
**Balance Sheet**  
June 30, 2002

Assets	Education Finance Funds				
	1983 General Bond Resolution	1997 General Bond Resolution	Line of Credit	Operating Fund	Combined Totals
<b>Current Assets:</b>					
Cash and Cash Equivalents	\$27,331,586	\$5,924,929	\$188,473	\$4,214,111	\$37,659,099
Investments	36,335,929			7,175,331	43,511,260
Accounts Receivable and Prepaid Expenses	17,607	70,439		836,331	924,377
Accrued Interest Receivable	3,787,869	16,144,249	280	4,485	18,936,883
Special Allowance Receivable	981,943	271			982,214
Interfund Receivable (Payable)	(887,189)	(1,603,010)	(23,387)	2,313,586	
<b>Total Current Assets</b>	<b>67,767,745</b>	<b>19,536,878</b>	<b>165,366</b>	<b>14,543,844</b>	<b>102,013,833</b>
<b>Noncurrent Assets:</b>					
Loans, Net	168,112,504	547,956,481			716,068,985
Cash and Cash Equivalents		68,331,429			68,331,429
Deferred Bond Issuance Costs, Net	789,986	3,132,850			3,922,836
Deferred Loan Purchase Premiums and Origination Costs, Net	808,644	6,793,641			7,602,285
Property, Plant and Equipment, Net				1,510,176	1,510,176
<b>Total Noncurrent Assets</b>	<b>169,711,114</b>	<b>626,214,401</b>		<b>1,510,176</b>	<b>797,435,691</b>
<b>Total Assets</b>	<b>\$237,478,859</b>	<b>\$645,751,279</b>	<b>\$165,366</b>	<b>\$16,054,020</b>	<b>\$899,449,524</b>
<b>Liabilities</b>					
<b>Current Liabilities:</b>					
Accounts Payable and Accrued Expenses	\$189,358	\$608,362	\$20,889	\$1,973,639	\$2,792,248
Accrued Interest Payable	487,959	813,559			1,301,518
Revenue Bonds/Note Payable	30,540,000				30,540,000
<b>Total Current Liabilities</b>	<b>31,217,317</b>	<b>1,421,921</b>	<b>20,889</b>	<b>1,973,639</b>	<b>34,633,766</b>
<b>Noncurrent Liabilities:</b>					
Revenue Bonds/Note Payable	133,230,000	625,000,000			758,230,000
Allowance for Arbitrage Liabilities	26,771,470	1,214,401			27,985,871
<b>Total Noncurrent Liabilities</b>	<b>160,001,470</b>	<b>626,214,401</b>			<b>786,215,871</b>
<b>Total Liabilities</b>	<b>191,218,787</b>	<b>627,636,322</b>	<b>20,889</b>	<b>1,973,639</b>	<b>820,849,637</b>
<b>Net Assets:</b>					
Invested in Capital Assets				1,510,176	1,510,176
Restricted	46,260,072	18,114,957	144,477		64,519,506
Unrestricted				12,570,205	12,570,205
<b>Total Net Assets</b>	<b>46,260,072</b>	<b>18,114,957</b>	<b>144,477</b>	<b>14,080,381</b>	<b>78,599,887</b>
<b>Total Liabilities and Net Assets</b>	<b>\$237,478,859</b>	<b>\$645,751,279</b>	<b>\$165,366</b>	<b>\$16,054,020</b>	<b>\$899,449,524</b>

The accompanying notes are an integral part of the financial statements.

**Kentucky Higher Education Student Loan Corporation**  
**Statement of Revenues, Expenses, and Changes in Net Assets**  
Year ended June 30, 2002

	<b>Education Finance Funds</b>				
	<b>1983 General Bond Resolution</b>	<b>1997 General Bond Resolution</b>	<b>Line of Credit</b>	<b>Operating Fund</b>	<b>Combined Totals</b>
<b>Revenues:</b>					
Interest Income:					
Loans	\$12,445,679	\$31,123,352	\$195,373		\$43,764,404
Special Allowance	3,923,877	50,369			3,974,246
Investments	2,250,163	2,315,987	18,456	\$268,654	4,853,260
Commission on Debt Recovery				1,596,669	1,596,669
Servicing Fees				2,181,053	2,181,053
<b>Total Revenues</b>	<b>18,619,719</b>	<b>33,489,708</b>	<b>213,829</b>	<b>4,046,376</b>	<b>56,369,632</b>
<b>Expenses:</b>					
Interest on Debt	7,799,108	14,669,282	158,555		22,626,945
Amortization of Bond Issuance Costs	255,040	118,884			373,924
Variable Bond Credit Facility and Remarketing Fees	225,258	1,605,402	87,990		1,918,650
Provision for Arbitrage Liabilities	4,279,396	531,586			4,810,982
Amortization of Loan Purchase Premiums and Origination Costs	178,308	1,101,278			1,279,586
Depreciation and Amortization	104,512	270,031	1,702	254,462	630,707
Federal Consolidation Fees	572,752	734,921			1,307,673
Personnel and Professional Services	1,154,387	2,748,165	18,041	2,044,281	5,964,854
Technical Services	159,913	413,173	2,603	390,373	966,062
General Administrative Expenses	458,968	1,172,675	7,391	1,123,982	2,763,016
Other Expenses	245,247	641,270	(15,890)	207,611	1,078,238
<b>Total Expenses</b>	<b>15,432,889</b>	<b>24,006,667</b>	<b>260,392</b>	<b>4,020,689</b>	<b>43,720,637</b>
<b>Operating Income (loss)</b>	<b>3,186,830</b>	<b>9,483,041</b>	<b>(46,563)</b>	<b>25,687</b>	<b>12,648,995</b>
Transfer to the Kentucky Higher Education Assistance Authority	(3,000,000)				(3,000,000)
<b>Increase (decrease) in Net Assets</b>	<b>186,830</b>	<b>9,483,041</b>	<b>(46,563)</b>	<b>25,687</b>	<b>9,648,995</b>
Net Assets at Beginning of Year	46,073,242	8,631,916	191,040	14,054,694	68,950,892
<b>Net Assets at End of Year</b>	<b>\$46,260,072</b>	<b>\$18,114,957</b>	<b>\$144,477</b>	<b>\$14,080,381</b>	<b>\$78,599,887</b>

The accompanying notes are an integral part of the financial statements.

**Kentucky Higher Education Student Loan Corporation**  
**Statement of Cash Flows**  
Year ended June 30, 2002

	<b>Education Finance Funds</b>				
	<b>1983 General Bond Resolution</b>	<b>1997 General Bond Resolution</b>	<b>Line of Credit</b>	<b>Operating Fund</b>	<b>Combined Totals</b>
<b>Cash Flows from Operating Activities:</b>					
Principal Received on Loans	\$36,883,704	\$73,023,157			\$109,906,861
Interest on Loans	8,745,158	20,740,182	\$1,195,490		30,680,830
Special Allowance	3,287,424	83,126	(236)		3,370,314
Client Loan Receipts				\$334,272,296	334,272,296
Servicing Fees				1,906,561	1,906,561
Commission Received on Debt Recovery				1,611,954	1,611,954
Loans Purchased, Including Premiums	(20,154,241)	(33,706,274)		(80,321)	(53,940,836)
Loans Originated, Including Costs	(13,299,421)	(114,854,081)			(128,153,502)
Credit Facility Fees	(182,396)	(1,540,589)	(81,441)		(1,804,426)
Loan Receipts Remitted to Clients				(333,822,580)	(333,822,580)
Interfund Transfer of Loans		(29,971,407)	29,971,407		
Other Expenses	(2,181,947)	(5,418,441)	(231,389)	(3,814,914)	(11,646,691)
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>13,098,281</b>	<b>(91,644,327)</b>	<b>30,853,831</b>	<b>72,996</b>	<b>(47,619,219)</b>
<b>Cash Flows from Investing Activities:</b>					
Investment Income Received	2,550,115	2,327,401	26,497	271,159	5,175,172
Proceeds from Sales and Maturities of Investments	82,105,842	5,590,000		19,149,000	106,844,842
Purchases of Investments	(75,999,011)	(4,665,019)		(18,265,518)	(98,929,548)
<b>Net Cash Provided by Investing Activities</b>	<b>8,656,946</b>	<b>3,252,382</b>	<b>26,497</b>	<b>1,154,641</b>	<b>13,090,466</b>
<b>Cash Flows from Noncapital Financing Activities:</b>					
Proceeds from Debt Issued		150,000,000			150,000,000
Debt Issuance Costs		(674,494)			(674,494)
Debt Principal Payments	(36,965,000)		(32,600,000)		(69,565,000)
Interest on Debt	(8,048,610)	(15,221,958)	(534,981)		(23,805,549)
Transfer to the Authority	(3,000,000)				(3,000,000)
<b>Net Cash Provided by (Used in) Noncapital Financing Activities</b>	<b>(48,013,610)</b>	<b>134,103,548</b>	<b>(33,134,981)</b>		<b>52,954,957</b>
<b>Cash Flows from Capital and Related Financing Activities</b>					
Property, Plant and Equipment Acquired				(925,799)	(925,799)
<b>Net Cash Used in Capital and Related Financing Activities</b>				<b>(925,799)</b>	<b>(925,799)</b>
Net Increase (Decrease) in Cash and Cash Equivalents	(26,258,383)	45,711,603	(2,254,653)	301,838	17,500,405
Cash and Cash Equivalents at Beginning of Year	53,589,969	28,544,755	2,443,126	3,912,273	88,490,123
<b>Cash and Cash Equivalents at End of Year</b>	<b>\$27,331,586</b>	<b>\$74,256,358</b>	<b>\$188,473</b>	<b>\$4,214,111</b>	<b>\$105,990,528</b>

The accompanying notes are an integral part of the financial statements.

**Kentucky Higher Education Student Loan Corporation**  
**Reconciliation of Operating Income to Net Cash Provided by Operating Income**  
Year ended June 30, 2002

	Education Finance Funds				
	1983 General Bond Resolution	1997 General Bond Resolution	Line of Credit	Operating Fund	Combined Totals
Operating Income (loss)	\$3,186,830	\$9,483,041	(\$46,563)	\$25,687	\$12,648,995
Income and Expense Items not Affecting Cash Provided by (Used in) Operating Activities:					
Investment Income	(2,550,115)	(2,327,401)	(26,497)	(271,159)	(5,175,172)
Depreciation and Amortization	104,512	270,031	1,702	254,462	630,707
Amortization of Bond Issuance Costs	255,040	115,678			370,718
Amortization of Loan Purchase Premiums and Origination Costs	178,308	1,101,278			1,279,586
Interest on Debt	7,799,108	14,669,282	158,555		22,626,945
Provision for Loan Losses	(52,162)	143,560	(22,039)	80,540	149,899
Borrower Interest Converted to Principal	(3,525,924)	(8,824,094)	100,464	(220)	(12,249,774)
Net Change in Fair Value of Investments	14,616	999		(2,894)	12,721
Items Not Accounted for as Revenues or Expenses:					
Principal Received on Loans	36,883,704	73,023,157			109,906,861
Loans Purchased, including Premiums	(20,154,241)	(33,706,274)		(80,321)	(53,940,836)
Loans Originated, including Costs	(13,299,421)	(114,854,081)			(128,153,502)
Interfund Transfer of Loans		(29,971,407)	29,971,407		
(Increase) Decrease in Assets:					
Accounts Receivable and Prepaid Expenses	1,371	115,227	26,559	(236,058)	(92,901)
Accrued Interest Receivable	83,652	(1,676,030)	907,517	5,399	(679,462)
Special Allowance Receivable	(636,453)	32,758	8		(603,687)
Interfund Receivable/Payable	431,673	117,464	(164,386)	(384,751)	
Increase (Decrease) in Liabilities:					
Accounts Payable and Accrued Expenses	99,072	110,898	(52,896)	682,311	839,386
Allowance for Arbitrage Liabilities	4,278,711	531,586			4,810,297
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>\$13,098,281</b>	<b>(\$91,644,327)</b>	<b>\$30,853,831</b>	<b>\$72,996</b>	<b>(\$47,619,219)</b>

The accompanying notes are an integral part of the financial statements.

## Kentucky Higher Education Student Loan Corporation

### Notes to Financial Statements

#### (1) Description of Business and General Bond Resolutions

The Kentucky Higher Education Student Loan Corporation (Corporation) is an independent *de jure* municipal corporation established by the Kentucky General Assembly in 1978 to provide a loan finance program for post-secondary students in the Commonwealth of Kentucky. Governed by a Board of Directors, the Corporation is authorized to finance loans for students attending eligible post-secondary institutions, service and collect education loans, and issue bonds and notes not to exceed \$1,950 million in order to carry out its corporate powers and duties. The Corporation's education finance, servicing and collection, activities include: (i) the origination and secondary market acquisition of education loans originated pursuant to the Federal Family Education Loan Program (FFELP); (ii) the financing of FFELP Loans; (iii) the servicing of FFELP Loans and of other education loans, and (iv) the collection of FFELP Loans and other education loans for other holders on a commission or cost reimbursement basis. The FFELP student loans held, serviced and collected by the Corporation include Federal Stafford Loans (Stafford), Unsubsidized Stafford Loans (Unsubsidized Stafford), Federal Supplemental Loans for Students (SLS), Federal Parent Loans for Undergraduate Students (PLUS), and Federal Consolidation Loans (Consolidations).

These FFELP loans are insured by the Kentucky Higher Education Assistance Authority (Authority), as the state guarantee agency, or the U. S. Department of Education (USDE). Loans made prior to October 1, 1993, are 100% insured. Loans made on or after October 1, 1993, are 100% insured against borrowers' death, disability, or bankruptcy and 98% insured against borrowers' default.

The Corporation's General Bond Resolutions (GBRs) and separate Series Resolutions for issue of revenue bonds contain provisions establishing funds and accounts for the segregation of assets and provisions restricting the use of the proceeds of bonds and other funds received.

As of June 30, 2002 the Corporation serviced approximately \$716 million outstanding principal amount of FFELP Loans which are pledged pursuant to the 1983 GBR, the 1997 GBR or the 2000 Line of Credit Trust Agreement and approximately \$2,931 million of FFELP Loans and other education loans on behalf of other holders, including holders with national lending operations. The majority of such education loans are being serviced by the Corporation pursuant to servicing agreements which do not provide for the acquisition by the Corporation of the education loans serviced. As a servicer of FFELP loans, the Corporation collects student loan remittances and subsequently disburses these remittances to the appropriate lending entities. In addition, the Corporation currently collects approximately \$105 million of FFELP Loans and other education loans for other holders on a commission or cost reimbursement basis. The Corporation's obligations pursuant to such servicing and collection agreements are without recourse to assets pledged to collateralize any Corporation financings.

## Kentucky Higher Education Student Loan Corporation

### Notes to Financial Statements

#### (2) Summary of Significant Accounting Policies

##### (a) Reporting Entity

The Corporation is a component unit agency of the Commonwealth of Kentucky and is reported as such in the Commonwealth of Kentucky Comprehensive Annual Financial Report.

##### (b) Basis of Presentation

In June 1999, the Governmental Accounting Standard Board (GASB) adopted GASB statement No. 34, "Basic Financial Statements and Management Discussion and Analysis – for State and Local Governments" as amended by GASB No. 37 and modified by GASB No. 38 "Certain Financial Statement Disclosures" (collectively, GASB 34.) The Corporation has adopted GASB 34 as required for the year ended June 30, 2002. The adoption of GASB 34 required the Corporation to make several changes to the presentation of its basic financial statements in addition to requiring the presentation of the Corporation's Management Discussion and Analysis (MD&A). MD&A is considered to be required supplemental data and precedes the financial statements.

In order to conform to the requirements of these statements, the following changes have been made to the Corporation's financial statements:

- Net Assets have been reclassified into the following categories:
  - Invested in Capital Assets
  - Restricted
  - Unrestricted
- The Balance Sheet has been modified to report a classified Balance Sheet.

The Corporation's basic financial statements prepared in accordance with GASB 34 are comprised of fund financial statements and notes to the financial statements. The fund financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America applicable to state government entities, which provide that financial activities operated similarly to private business enterprises be presented as separate proprietary funds and that accounting results be organized by funds to account for specific activities consistent with legal and operating requirements. The Corporation's funds include the Education Finance Funds and the Operating Fund. The Education Finance Funds include loan programs funded individually under financings under the 1983 GBR, the 1997 GBR and the 2000 Line of Credit.



## Kentucky Higher Education Student Loan Corporation

### Notes to Financial Statements

#### (2) Summary of Significant Accounting Policies (continued)

Financial activities operated similarly to private business enterprises and financed through fees for servicing and defaulted loan collection are presented under the Operating Fund. The Corporation follows all applicable Governmental Accounting Standards Board pronouncements, as well as Financial Accounting Standards Board pronouncements and Accounting Principles Board Opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The Corporation uses the accrual basis of accounting.

##### (c) Loan Losses

As discussed in Note 1, the FFELP loans are guaranteed by the Authority. Management of the Corporation believes that the Authority will be able to honor all default claims presented by the Corporation. However, the Corporation records a provision for loan losses based upon its expected default claims with respect to 98% insured loans. The allowance for loan losses was \$963,046 for loan principal and \$135,697 for accrued interest as of June 30, 2002.

##### (d) Investments

Investments, which consist principally of securities of the federal government or its agencies and commercial paper, are reported at fair market value. Fair market value is determined by using quoted market prices as of the last day of the fiscal year.

##### (e) Interest Income on Loans

The Corporation earns interest income on loans from three sources: (1) the USDE for subsidized interest earned while the student is in school; (2) special allowance subsidies (discussed in Footnote 6); and (3) the borrowers. All interest is recorded when earned and is shown in the financial statements net of the interest portion of the provision for loan losses.

##### (f) Commission on Debt Recovery

The Corporation's fee for collection of defaulted education loans is recorded as commission revenue when payments are received. Defaulted loans are not presented on the balance sheet as they are not owned by the Corporation.

##### (g) Servicing Fees

The Corporation's fee for servicing loans held by third parties is recorded as servicing fee revenue when earned. These third-party loans are not presented on the balance sheet as they are not owned by the Corporation.

# Kentucky Higher Education Student Loan Corporation

## Notes to Financial Statements

### (2) Summary of Significant Accounting Policies (continued)

#### (h) Income Taxes

The Corporation is an independent *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky and is therefore not subject to federal or state income taxes.

#### (i) Deferred Bond Issuance Costs

Bond issuance costs are deferred and amortized over the life of the bonds, utilizing the bonds outstanding method, which approximates the effective interest method.

#### (j) Deferred Loan Purchase Premiums and Deferred Loan Origination Costs

Loan purchase premiums and certain origination costs are deferred and amortized over the estimated life of the loans acquired or originated, based on projected balances outstanding, which approximates the effective interest method.

#### (k) Interfund Eliminations

Interfund receivables and payables are eliminated in the balance sheet.

#### (l) Property, Plant and Equipment

Office furnishings, equipment, and system development costs are depreciated over their estimated useful lives using the straight-line method.

#### (m) Statement of Cash Flows

For the statement of cash flows, the Corporation considers cash and cash equivalents to include money market funds and investments which mature within one month of purchase.

#### (n) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

### (2) Cash, Cash Equivalents and Investments

Cash, cash equivalents and investments as of June 30, 2002, are summarized below:

Investments	\$43,511,260
Cash Equivalents	105,477,743
Cash	512,785
Total Cash, Cash Equivalents and Investments	<u>\$149,501,788</u>

# Kentucky Higher Education Student Loan Corporation

## Notes to Financial Statements

### (3) Cash, Cash Equivalents and Investments (continued)

Deposits, identified as cash in the above summary, are as follows as of June 30, 2002:

	Financial Statement Amount	Bank Balance
Insured (FDIC)	\$200,000	\$200,000
Collateralized		
Uninsured and uncollateralized	312,785	999,432
Total Deposits	<u>\$512,785</u>	<u>\$1,199,432</u>

The following is a summary of investments, including cash equivalents, categorized as of June 30, 2002:

	Category 1	Uncategorized	Total
U.S. Treasury and Government Agency Obligations	\$43,825,739		\$ 43,825,739
Government Mutual Funds		\$29,809,807	29,809,807
Money Market Securities		75,353,457	75,353,457
Total Investments	<u>\$43,825,739</u>	<u>\$105,163,264</u>	<u>\$148,989,003</u>

The Corporation's investments are categorized to give an indication of the level of risk assumed by the Corporation at year-end. Category 1 includes investments that are insured, registered, or for which the securities are held by the Corporation or its agent in the Corporation's name. As of June 30, 2002 the Corporation did not have any Category 2 or 3 investments.

### (4) Loans

The Corporation originates, purchases and holds various types of student loans as described in Note 1. The terms of these loans, which vary on an individual basis depending upon loan type and the date the loan was originated, generally provide for repayment in monthly installments of principal and interest over a period of up to thirty years for Consolidation loans and generally up to ten years for other loans. The repayment period begins after a grace period of six months following graduation or loss of qualified student status for the Subsidized and Unsubsidized Stafford loans. The repayment period for Consolidation, SLS and PLUS loans begins within 60 days from the date the loan is fully disbursed. Interest rates on student loans ranged from 4.45% to 12.00% for the fiscal year ended June 30, 2002 depending upon the type and date of origination of the individual loan.

**Kentucky Higher Education Student Loan Corporation**  
**Notes to Financial Statements**

(4) Loans (continued)

Loans consist of the following at June 30, 2002:

Stafford – Subsidized	\$348,184,252
Stafford – Unsubsidized	207,657,421
PLUS/SLS	21,630,040
Consolidation	139,454,416
Other	105,902
Total gross loans	717,032,031
Allowance for loan loss	(963,046)
Net loans	\$716,068,985
Net deferred premium and loan cost	7,602,285
Net Loans and deferred premium and loan costs	<u>\$723,671,270</u>

All FFELP student loans are guaranteed as to principal and accrued interest by the Authority. In order for the loans to be or remain guaranteed, certain due diligence requirements in loan servicing must be met. As of June 30, 2002, \$1,257,143 of loans were no longer considered guaranteed.

The Corporation withholds certain origination fees from the loan disbursements on FFELP loans to the borrowers and remits these fees to USDE. The amount of the origination fees is based on a percentage of the gross loan amount.

The Corporation is also required to pay to USDE certain Lender and Rebate Fees. The amount of the Lender Fees is based on a certain percentage of the gross loan amount on all FFEL Program loans originated after October 1, 1993 and a certain percentage of the carrying value of the Consolidation loans.

Loan origination costs are capitalized when the loan is made and are amortized, using the effective interest method, over the estimated economic life of the loan. The capitalized loan origination costs, net of accumulated amortization, at June 30, 2002, were approximately \$5,884,449.

Generally, student loans of the Corporation are pledged as collateral for the various obligations of the Corporation.

# Kentucky Higher Education Student Loan Corporation

## Notes to Financial Statements

### (5) Property, Plant and Equipment

A summary of Property, Plant and Equipment follows:

	Beginning Balance July 1, 2001	Additions	Disposals	Ending Balance June 30, 2002
Furniture	\$ 929,224	\$ 27,127	\$ 1,342	\$ 955,009
Computer Equipment	1,974,009	761,178	120,253	2,614,934
Other Equipment	164,930	33,776	932	197,774
System Development - Information Services	55,955			55,955
Student Loan Servicing System	436,131	105,000		541,131
Debt Recovery System	139,350			139,350
Tuition Line Servicing System	16,922			16,922
Total Property, Plant and Equipment	\$ 3,716,521	\$ 927,081	\$ 122,527	\$ 4,521,075
Total Accumulated Depreciation	(2,501,437)	(630,707)	(121,245)	(3,010,899)
Net Property, Plant and Equipment	\$ 1,215,084	\$ 296,374	\$ 1,282	\$ 1,510,176

### (6) Special Allowance

The U.S. Department of Education pays a special allowance to the Corporation after the end of each quarter representing supplemental interest on outstanding, insured loans. Stafford Loans disbursed during the period from January 1, 2000 through June 30, 2003, receive special allowance at a rate based upon the average of the bond equivalent rates of the 3-month commercial paper rate as reported by the U.S. Federal Reserve. Other eligible loans receive special allowance based on the 91-day U.S. Treasury bill rates.

### (7) Retirement Plan

The Corporation provides retirement benefits to all full-time employees through the Kentucky Employees Retirement System (KERS). KERS is a multiple-employer, defined benefit plan sponsored by the Commonwealth of Kentucky, which provides retirement, disability, and death benefits. The Corporation contributed 5.89% of gross wages for the year ended June 30, 2002. The employees contributed 5% of their gross wages to the plan for the years ended June 30, 2002. Such rates are intended to provide for normal costs on a current basis, plus an amount equal to the amortization of unfunded past service costs over thirty years, using the level percentage of payroll method. These contribution rates are determined by the Board of Trustees of KERS each biennium. The payroll of employees covered by the retirement plan was \$4,376,401 for the year ended June 30, 2002. Total payroll for the year ended June 30, 2002 was \$4,813,789. KERS participants have fully vested interests after the completion of sixty months of service, twelve months of which are current service. The KERS contribution requirement for the year ended June 30, 2002 was \$476,597, which consisted of employer contributions of \$257,774 and \$218,823 from employees in 2002. Although separate measurements of assets and pension benefit obligation are not available for individual employers, KERS's annual financial report (which is a matter of public record) contains this information for KERS as a whole.

# Kentucky Higher Education Student Loan Corporation

## Notes to Financial Statements

### (8) Revenue Bonds

The balance of revenue bonds at June 30, 2002 and the related activity for the year ended June 30, 2002 is as follows (in thousands):

Series	Scheduled Maturity	Interest Rate	Beginning Balance @ July 1, 2001	Bond Maturities	New Issues	Ending Balance @ June 30, 2002
<b><u>1983 General Bond Resolution</u></b>						
1991 B	Semi-annually in various amounts through June 1, 2003	6.80%	\$ 5,360	\$ (3,760)		\$ 1,600
1991 C	Semi-annually in various amounts through June 1, 2002	6.50%	5,000	(5,000)		
1991 D	Semi-annually in various amounts through December 1, 2011	6.75% to 7.10%	7,600	(480)		7,120
1991 E	December 1, 2011	Weekly**	46,000			46,000
1993 B	Semi-annually in various amounts through December 1, 2005	4.90% to 5.30%	90,000	(14,200)		75,800
1993 C	June 1, 2002	5.15%	1,130	(1,130)		
1994 A	June 1, 2002	6.25%	4,500	(4,500)		
1994 B	June 1, 2002	6.60%	3,435	(3,435)		
1995 A	June 1, 2002	4.90%	2,655	(2,655)		
1995 B	June 1, 2003	5.15%	750			750
1995 C	June 1, 2003	5.45%	3,000			3,000
1996 A	June 1, 2026	Weekly**	25,000			25,000
1996 B	June 1, 2003	5.15%	2,500			2,500
1997 A	June 1, 2002	4.90%	1,160	(1,160)		
1997 B	June 1, 2003	5.15%	1,000			1,000
1997 C	June 1, 2002	5.15%	645	(645)		
1997 D	June 1, 2003	5.40%	1,000			1,000
<b><u>1997 General Bond Resolution</u></b>						
1997 A-1	May 1, 2027	Every 35 days**	45,250			45,250
1997 A-2	May 1, 2027	Every 35 days**	45,200			45,200
1997 B	May 1, 2027	Every 35 days**	44,550			44,550
1998 A-1	May 1, 2028	Every 28 days**	36,400			36,400
1998 A-2	May 1, 2028	Every 28 days**	36,400			36,400
1998 B	May 1, 2028	Every 35 days**	42,200			42,200
1999 A	May 1, 2029	Every 28 days**	51,350			51,350
1999 B	May 1, 2029	Every 35 days**	23,650			23,650
2000 A-1	May 1, 2030	Every 28 days**	42,100			42,100
2000 A-2	May 1, 2030	Every 28 days**	42,100			42,100
2000 A-3	May 1, 2030	Every 35 days**	42,050			42,050
2000 B	May 1, 2030	Every 35 days**	23,750			23,750
2001 A-1	May 1, 2031	Every 35 days**			\$ 59,850	59,850
2001 A-2	May 1, 2031	Every 35 days**			59,850	59,850
2001 B	May 1, 2031	Every 35 days**			30,300	30,300
			<b>\$ 675,735</b>	<b>\$ (36,965)</b>	<b>\$ 150,000</b>	<b>\$ 788,770</b>

\*\* Variable interest rate changes based on specified indices.

All Revenue Bonds except for the Senior Series 1997-A-1 and 1997-A-2, Senior Series 1998A-1 and 1998A-2, Senior Series 1999A, and Senior Series 2000A-1, 2000A-2, and Senior Series 2000A-3 and Senior Series 2001A-1 and 2001A-2 are tax-exempt issues.

**Kentucky Higher Education Student Loan Corporation**  
**Notes to Financial Statements**

(8) Revenue Bonds (continued)

Debt service requirements to maturity or redemption date, assuming interest rates on variable rate debt remains at June 30, 2002 levels, are as follows:

	<u>Principal Repayment Amount (Thousands)</u>		
	<u>83 GBR</u>	<u>97 GBR</u>	<u>Total</u>
Year Ending June 30, 2003	\$ 30,540		\$ 30,540
Year Ending June 30, 2004	19,715		19,715
Year Ending June 30, 2005	37,680		37,680
Year Ending June 30, 2006	845		845
Year Ending June 30, 2007	995		995
5 Years Ending June 30, 2012	48,995		48,995
5 Years Ending June 30, 2027	25,000	\$ 135,000	160,000
4 Years Ending June 30, 2031		490,000	490,000
	<u>\$ 163,770</u>	<u>\$ 625,000</u>	<u>\$ 788,770</u>

	<u>Interest Payments Amount (Thousands)</u>		
	<u>83 GBR</u>	<u>97 GBR</u>	<u>Total</u>
Year Ending June 30, 2003	\$ 6,045	\$ 16,809	\$ 22,854
Year Ending June 30, 2004	4,522	16,809	21,331
Year Ending June 30, 2005	3,435	16,809	20,244
Year Ending June 30, 2006	1,814	16,809	18,623
Year Ending June 30, 2007	1,752	16,809	18,561
5 Years Ending June 30, 2012	7,359	84,047	91,406
5 Years Ending June 30, 2017		86,670	86,670
5 Years Ending June 30, 2022		86,670	86,670
5 Years Ending June 30, 2027		85,848	85,848
4 Years Ending June 30, 2031		35,879	35,879
	<u>\$ 24,927</u>	<u>\$ 463,159</u>	<u>\$ 488,086</u>

All assets of the 1983 General Bond Resolution Fund and 1997 General Bond Resolution Fund are pledged for repayment of the specific bond issues under each resolution.

(9) Line of Credit

On November 1, 2000, the Corporation increased its Line of Credit Agreement Note with Bank of America, N.A., providing for advances to the Corporation not to exceed an aggregate outstanding principal balance of \$100 million. The borrowing period ends December 31, 2002, and can be extended at the discretion of both parties through December 31, 2003. During the year ended June 30, 2002, the Corporation made principle payments of \$32,600,000 on this line of credit and at June 30, 2002, there were no advances outstanding.

## **Kentucky Higher Education Student Loan Corporation**

### **Notes to Financial Statements**

#### **(10) Allowance for Arbitrage Liabilities**

Certain of the Corporation's tax-exempt bond issues subject the Corporation to potential arbitrage liabilities under U.S. tax law. Arbitrage liabilities, under current federal income tax law regarding tax-exempt bond issues, consist of three types; (1) yield adjustment payments, (2) forgiveness and (3) arbitrage rebate. At June 30, 2002, the Corporation is reporting a liability for yield adjustment payments and forgiveness of \$27,400,116 and for arbitrage rebate of \$585,755.

The determination of excess yield on acquired purpose investments is cumulative over the life of the applicable bond series, as is the determination of arbitrage rebate on non-purpose investments, except for variable rate bonds for which arbitrage rebate is generally determined for each five-year period without retroactivity.

Yield adjustment payments, which also relate to yield restriction on acquired purpose investments, are applicable to the 1991 Series D & E Bonds, 1996 Series A, Subordinate Series 1997-B, Senior Series 1998B, Senior Series 1999B, Senior Series 2000B, Senior Series 2001B, and any future issues except certain refunding issues. The allowable yield is 2% above the bond yield (arbitrage yield), with the federal special allowance included in income. The loss of tax-exempt status may be avoided by rebating the excess yield to the U.S. Treasury every 10 years, and upon final maturity of the bonds.

Forgiveness is applicable to the 1991 Series B & C, 1993 Series A, B & C, 1994 Series A & B, 1995 Series A, B & C, 1996 Series B, and 1997 Series A, B, C, & D bonds. In general, a yield restriction is imposed on acquired purpose investments, designating the allowable yield as 1.5% above the bond yield (arbitrage yield), with the federal special allowance excluded from income. The loss of tax-exempt status may be avoided by partial forgiveness of the applicable student loans. Forgiveness can be applied upon maturity of the bonds or as otherwise prescribed by the bond resolutions.

Arbitrage rebate is applicable to all of the Corporation's tax-exempt bonds except the 1985 Series A. With certain limited exceptions, income earned on non-purpose investments (investments other than student loans), which exceeds the bond yield (arbitrage yield), must be rebated to the U.S. Treasury. Payments of at least 90% are due every five years after the year of issuance, and upon final maturity of bonds.

#### **(11) Credit and Liquidity Facilities and Bond Remarketing**

The 1991 Series E and 1996 A Bonds are collateralized with Standby Bond Purchase Agreements, pursuant to which Landesbank Hessen-Thüringen Girozentrale will purchase any bonds not remarketed. The 1991 Series E Bonds and the 1996 Series A Bonds also have a Municipal Bond Insurance Policy issued by AMBAC Indemnity Corporation and MBIA Insurance Corporation, respectively, which collateralizes payment of principal and interest on the bonds. The Standby Bond Purchase Agreements expires June 13, 2003, unless it is



## Kentucky Higher Education Student Loan Corporation

### Notes to Financial Statements

#### (11) Credit and Liquidity Facilities and Bond Remarketing (continued)

renewed, the AMBAC Municipal Bond Insurance Policy extends through the term of the 1991 Series E Bonds, December 1, 2011 and the MBIA Municipal Bond Insurance Policy extends through the term of the 1996 Series A Bonds, June 1, 2026.

The Corporation pays certain fees with respect to its variable rate bonds to auction agents, broker dealers, market agents, remarketing agents, and tender agents for remarketing bonds or conducting auctions of bonds. These arrangements are generally cancellable with prior notice by either party.

#### (12) Related Party Transactions

The chairman and an *ex officio* non-voting member of the Authority's Board of Directors are voting members on the Corporation's Board of Directors. One member of the Authority's management serves in a similar capacity for the Corporation.

During the year ended June 30, 2002, the Corporation incurred expenses of \$435,786 for technical services and \$588,931 for document processing services provided by the Authority. For the year ended June 30, 2002, the Corporation also incurred expenses of \$198,273 for loan origination and disbursement services provided by the Authority. Pursuant to a separate agreement, the Corporation collects certain defaulted student loans for the Authority. Fee revenue recognized with respect to loan collection services for the year ended June 30, 2002 was \$1,358,600.

The amount due to the Authority at June 30, 2002 was \$96,575. The amount due from the Authority at June 30, 2002 was \$25,641. Substantially all loans purchased or made by the Corporation are insured by the Authority.

During the year ended June 30, 2002, the Corporation made transfers totaling \$3 million to the Authority for support of state student financial aid programs, as approved by the Corporation's Board of Directors, pursuant to Section 508(c) of the 1983 General Bond Resolution.

Certain members of the Corporation's Board of Directors serve as officers or directors of lending institutions. In the normal course of business, the Corporation purchases loans from these institutions and the institutions refer borrowers to the Corporation for loans.

#### (13) Net Assets

Restricted net assets consist of net assets of the Education Finance Funds as required by the 1983 and 1997 General Bond Resolutions, the separate Series Resolutions, and Line of Credit Agreements. Pursuant to action of the Board of Directors, unrestricted net assets at June 30, 2002 includes \$8,246,041, representing a reservation of funds equal to one-half of the Corporation's budgeted operating expenses for the then upcoming fiscal year.

## **Kentucky Higher Education Student Loan Corporation**

### **Notes to Financial Statements**

#### **(14) Commitments and Contingencies**

The Corporation has entered into loan purchase contracts with various eligible lenders. Subject to the terms and conditions of these agreements, the Corporation on June 30, 2002, had plans to purchase approximately \$91 million of loans. These contracts cannot be terminated by either party.

#### **(15) Subsequent Events**

On July 18, 2002 the Governor of the Commonwealth of Kentucky issued Executive Order No. 2002-48. The Executive Order had the effect of making the membership of the KHESLC Board and the Authority's Board the same. For the year ended June 30, 2003 KHESLC will be considered a component unit of the Authority as a result of the changes that resulted from the Executive Order.

On July 25, 2002 the Corporation received an additional \$27,580,012 allocation from the Kentucky Private Activity Bond Allocation Committee. This will enable the Corporation to issue additional tax-exempt debt by December 2002 or to carryover for use in early 2003.

On September 27, 2002 the Corporation and Bank of America agreed to extend the Line of Credit Agreement through December 31, 2003.

**Appendix E**

**Proposed Form of Approving Opinion  
of Bond Counsel**

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## APPENDIX E

### PROPOSED FORM OF APPROVING OPINION OF BOND COUNSEL

Bond Counsel proposes to deliver its final approving opinion upon the delivery of the Senior Series 2003A-1 Bonds and Senior Series 2003A-2 Bonds, in substantially the form that follows.

#### [ LETTERHEAD OF HAWKINS, DELAFIELD & WOOD ]

May \_\_, 2003

Kentucky Higher Education Student  
Loan Corporation  
Louisville, Kentucky

Ladies and Gentlemen:

We have examined a record of proceedings relating to the issuance of \$80,650,000 Student Loan Revenue Bonds, Senior Series 2003A-1 and Senior Series 2003A-2 (the “Senior Series 2003A-1 Bonds” and the “Senior Series 2003A-2 Bonds”, respectively, and, collectively, the “Senior Series 2003A Bonds”), of the Kentucky Higher Education Student Loan Corporation (the “Corporation”), a public body corporate and politic constituting an independent *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky.

The Senior Series 2003A Bonds have been authorized and issued pursuant to Chapter 164A of the Kentucky Revised Statutes, as amended (the “Act”), a 1997 General Bond Resolution adopted by the Corporation on May 9, 1997, as amended (the “General Resolution”), and the Series 2003A-1 and Series 2003A-2 Bond Resolution which specifically authorized the Senior Series 2003A Bonds (the “Series Resolution”), approved by operation of the authorizing resolutions adopted by the Corporation on February 5, 2003 and May 6, 2003 (the “Authorizing Resolutions”). Certain capitalized terms used but not defined herein are as defined for purposes of the Series Resolution. Pursuant to the General Resolution, the Authorizing Resolutions and the Series Resolution, the Corporation has authorized the issuance of the Senior Series 2003A-1 Bonds for the purposes of providing funds for the financing of Student Loans and has authorized the issuance of the Senior Series 2003A-2 Bonds for the purposes of providing funds for: (i) the payment of the principal of certain bonds of the Corporation issued pursuant to the Corporation’s 1983 General Bond Resolution adopted on June 10, 1983 (as heretofore amended, the “1983 General Bond Resolution”) and due and payable on June 1, 2003; and (ii) the payment of principal of a certain interim financing the proceeds of which were used to refund on December 1, 2002 certain bonds of the Corporation issued pursuant to the 1983 General Bond Resolution. The Corporation has delivered to the Trustee a Supplemental Resolution Adopted May 6, 2003 (the “2003 Supplemental Resolution”) which will amend certain provisions of the General Resolution, upon its effective date of May \_\_, 2003.

The Senior Series 2003A Bonds, dated as of the date of the initial issuance thereof, are scheduled to mature on the dates and in the principal amounts and will bear interest at the rates, and be payable on the dates, determined as provided in the Series Resolution.

The Senior Series 2003A Bonds are issuable as fully registered bonds in the denomination of \$50,000 and any integral multiple thereof. The Senior Series 2003A Bonds are subject to exchange, to conversion, to mandatory tender and to redemption prior to maturity and are payable upon the terms and conditions set forth therein, in the General Resolution and in the Series Resolution.

Pursuant to the Act, the General Resolution and the Authorizing Resolutions, the Corporation is authorized to issue the Senior Series 2003A Bonds. The Senior Series 2003A Bonds constitute Senior Obligations entitled to the equal benefit, protection and security of the provisions and covenants of the General Resolution and the Series Resolution with respect to Senior Obligations.

The General Resolution and the Series Resolution provide that the pledges and assignments made thereby and the provisions, covenants and agreements of the Corporation therein set forth shall be for the equal benefit, protection and security of the Owners of any and all Obligations, each of which shall be of equal rank without preference, priority or distinction, except as expressly provided therein. The General Resolution and the Series Resolution further provide that the Senior Series 2003A Bonds and all other Senior Obligations shall have the same priority of claim as to payment under the General Resolution, which priority shall be Senior to that of all Obligations other than Senior Obligations. The Corporation reserves the right to issue Additional Obligations under the General Resolution which are equal to or subordinate in such priority to the Senior Series 2003A Bonds.

The General Resolution and the Series Resolution provide that nonpayment of the principal of or interest on Subordinate Obligations, including Senior Subordinate Obligations, occurring while any Obligations which are senior in priority of claim as to payment under the General Resolution and the Series Resolution to the Obligations affected, and which are not affected by such nonpayment, remain Outstanding, shall not result in an Event of Default under the General Resolution and the Series Resolution that would give rise to a right on the part of Owners of affected Obligations to accelerate the affected Obligations or to exercise any other remedy. The General Resolution and the Series Resolution further provide: (i) that only Owners of Obligations which are not subordinate in priority of claim as to payment thereunder to any other Outstanding Obligations, such as the Senior Series 2003A Bonds, may exercise any remedy or right of enforcement or consent to any action thereunder; and (ii) that the exercise by such Owners of the remedy of acceleration in response to an Event of Default which does not result from nonpayment of the principal of or interest on Obligations is conditioned upon the consent of all Owners of Outstanding Obligations.

The General Resolution and the Series Resolution provide that Owners of the Senior Series 2003A Bonds will have no claim to any amounts properly distributed from the Trust Estate from time to time pursuant to the General Resolution and that the recipients of such amounts shall in no event be required to refund such distributed amounts.

We are of the opinion that:

1. The Corporation is a duly organized and existing independent *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky, pursuant to the Constitution and laws of the Commonwealth of Kentucky.

2. The Corporation has valid right and lawful authority to adopt the General Resolution, the Authorizing Resolutions and the Series Resolution, to issue its Student Loan Revenue Bonds, including the Senior Series 2003A Bonds, pursuant to the General Resolution, the Authorizing Resolutions and the Series Resolution and to perform its duties, obligations and covenants pursuant to the terms and conditions of the General Resolution and the Series Resolution including the financing and refinancing of Student Loans.

3. The General Resolution, the Authorizing Resolutions and the Series Resolution have been duly and validly adopted by the Corporation, are in full force and effect and are valid and binding upon the Corporation and enforceable in accordance with their terms, except that the 2003 Supplemental Resolution has not yet become effective.

4. The Senior Series 2003A Bonds have been duly authorized and issued by the Corporation in accordance with the Constitution and laws of the Commonwealth of Kentucky, the General Resolution, the Authorizing Resolutions and the Series Resolution.

5. The Senior Series 2003A Bonds are valid and binding special and limited obligations of the Corporation, enforceable in accordance with their terms and the terms of the General Resolution and the Series Resolution and entitled to the benefits of the Act, the General Resolution, the Authorizing Resolutions and the Series Resolution. As provided by the General Resolution, the Senior Series 2003A Bonds are secured by a pledge of certain revenues, assets and funds of the Corporation, including: (i) the proceeds of the sale of the Senior Series 2003A Bonds; (ii) the Revenues and Loans; and (iii) all moneys and investments held in any of the funds and accounts established by the General Resolution (other than the Rebate Fund), subject to the provisions of the General Resolution and the Series Resolution permitting the use, application and disposal thereof. Pursuant to

Section 164A.100 of the Act, such pledge is valid and binding and the lien of such pledge as security for the payment of the Senior Series 2003A Bonds, on a basis of parity with all other Obligations secured thereby and subject to the provisions of the General Resolution and the Series Resolution permitting the use, application and disposal thereof, is valid and binding as against any and all parties having claims against the Corporation.

6. The Senior Series 2003A Bonds do not constitute a debt, liability or other obligation of the Commonwealth of Kentucky, and neither the faith and credit nor the taxing power of the Commonwealth of Kentucky is pledged to the payment of the principal of or interest on the Senior Series 2003A Bonds.

7. Under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein, interest on the Senior Series 2003A Bonds is excluded from gross income for federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"). Interest on the Senior Series 2003A Bonds will be treated as a preference item in calculating the alternative minimum tax imposed under the Code on individuals and corporations.

The Code establishes certain requirements that must be met subsequent to the issuance and delivery of the Senior Series 2003A Bonds in order that interest on the Senior Series 2003A Bonds be and remain excluded from gross income under Section 103 of the Code. These requirements include, but are not limited to, requirements relating to the use and expenditure of Senior Series 2003A Bond proceeds, yield and other restrictions on the investment of Senior Series 2003A Bond proceeds prior to expenditure and the arbitrage rebate requirement that certain excess earnings on the Senior Series 2003A Bond proceeds be rebated to the federal government. Noncompliance with such requirements may cause interest on the Senior Series 2003A Bonds to become included in gross income for federal income tax purposes retroactive to their date of issue, irrespective of the date on which such noncompliance is ascertained.

The Corporation has covenanted to comply with certain applicable requirements of the Code to assure the exclusion of interest on the Senior Series 2003A Bonds from gross income under Section 103 of the Code.

In rendering the opinion in paragraph 7 hereof, we have relied upon and assumed: (i) the material accuracy of the representations, statements of intention and reasonable expectation and certifications of fact contained in the Tax Regulatory Agreement dated May \_\_, 2003 (the "Tax Regulatory Agreement") with respect to matters affecting the status of interest paid on the Senior Series 2003A Bonds; and (ii) compliance by the Corporation with the procedures and covenants set forth in the Tax Regulatory Agreement.

8. Under existing statutes, the Senior Series 2003A Bonds, the income thereon and the transfer thereof, including any profit made on the sale thereof, shall at all times be exempt from taxation or assessment of any type by the Commonwealth, its agencies and departments and by all political subdivisions within the Commonwealth.

In rendering this opinion, we are advising you that the enforceability of the Bonds, the General Resolution and the Series Resolution may be limited by bankruptcy, moratorium, insolvency or other laws affecting creditors' rights or remedies and is subject to general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

We express no opinion on the effect of any action hereafter taken or not taken in reliance upon an opinion of other counsel on the exclusion from gross income for federal income tax purposes of interest on the Senior Series 2003A Bonds, or under state and local tax law.

We have examined an executed Senior Series 2003A-1 Bond and an executed Senior Series 2003A-2 Bond and, in our opinion, the respective forms of said Senior Series 2003A-1 Bond and the Senior Series 2003A-2 Bond and their execution are regular and proper.

Very truly yours,

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## **Appendix F**

### **Auction Procedures for the Senior Series 2003A Bonds**

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## AUCTION PROCEDURES FOR THE SENIOR SERIES 2003A BONDS

*If not otherwise defined in this Appendix F, capitalized terms used in this Appendix F will have the meanings given such terms in the Resolutions (and described in Appendix C of this Official Statement). The procedures described in this Appendix F apply separately to each Subseries of the Senior Series 2003A Bonds and apply only while such Subseries is outstanding as ARCs.*

### Definitions

The following definitions apply to this Appendix F:

“AA’ Financial Commercial Paper Rate”, on any date of determination, means (a) for Auction Periods of 35 days or less, the interest equivalent of commercial paper having a maturity of 30 days, (b) for Auction Periods greater than 35 days and less than 75 days, the interest equivalent of commercial paper having a maturity of 60 days, (c) for Auction Periods greater than 75 days and less than 105 days, the interest equivalent of commercial paper having a maturity of 90 days; as each such rate is published on the Business Day prior to such date by the Board of Governors of the Federal Reserve System on its World Wide Web site <http://www.federalreserve.gov/releases/cp/histrates.txt>, or any successor publication (“H.15(519)”) under the caption “AA financial.” In the event that such publication has not been published in a timely manner, the “AA” Financial Commercial Paper Rate shall be calculated by the Market Agent, and shall be the bond equivalent yield of the arithmetic mean of the offered rates as of 11:00 a.m., New York City time, on the determination date of three leading dealers of U.S. dollar commercial paper in The City of New York (which may include UBS Paine Webber Inc.) selected by the Market Agent, for U.S. dollar commercial paper having a maturity of 30, 60 or 90 days, as applicable, placed for financial issuers whose bond rating is “AA” or the equivalent, from a nationally recognized securities rating agency; provided, however, that if the dealers selected as aforesaid by the Market Agent are not quoting as mentioned in this sentence (and if the Market Agent, in its discretion, determines that such quotations can not be obtained from any three leading dealers of U.S. dollar commercial paper in The City of New York) such rate shall be the same rate as in effect for the immediately preceding Interest Period.

For purposes of this definition, the “interest equivalent” of a rate stated on a discount basis (a “discount rate”) for commercial paper of a given day’s maturity shall be equal to the product of (A) 100 times (B) the discount rate (expressed in decimals) times (C) the quotient (rounded upwards to the next higher one-thousandth (.001) of 1%) of (x) the applicable number of days in a year (365 or 366) divided by (y) the difference between (1) 360 and (2) the product of the discount rate (expressed in decimals) times the applicable number of days in which such commercial paper matures.

“After-Tax Equivalent Rate”, on any date of determination, means the interest rate per annum equal to the product of:

- (i) the “AA” Financial Commercial Paper Rate on such date; and
- (ii) 1.00 minus the Statutory Corporate Tax Rate on such date.

“All Hold Rate”, on any date of determination, means the interest rate per annum equal to 90% (as such percentage may be adjusted pursuant to the Series 2003A Bond Resolution) of the lesser of:

- (a) the After Tax Equivalent Rate on such date; and
- (b) the Kenny Index on such date;

rounded to the nearest one-thousandth (0.001) of 1%; provided that in no event shall the All Hold Rate be more than the Maximum Rate or less than zero.

“Applicable ARCs Rate” means with respect to a series of ARCs the annual rate of interest that results from implementation of the Auction Procedures.

“Applicable Number of Business Days” means the greater of two Business Days or one Business Day plus the number of Business Days by which the Auction Date precedes the first day of the next succeeding Interest Period.

“Applicable Percentage”, on the date of determination, means the percentage determined (as such percentage may be adjusted pursuant to the Series 2003A Bond Resolution) based on the lower of the prevailing credit ratings on the ARCs in effect at the close of business on the Business Day immediately preceding such date, as set forth below:

<b>Moody’s</b>	<b>S&amp;P</b>	<b>Applicable Percentage</b>
“Aaa”	“AAA”	175%
“Aa3” to “Aa1”	“AA-” to “AA+”	175%
“A3” to “A1”	“A-” to “A+”	175%
“Baa3” to “Baa1”	“BBB-” to “BBB+”	200%
Below “Baa3”	Below “BBB-”	265%

provided, that, in the event that the ARCs are not rated by any nationally recognized rating agency, the Applicable Percentage shall be 265%; and provided further, that if a Payment Default shall have occurred and be continuing, the Applicable Percentage shall be 265%. For purposes of this definition, Moody’s rating categories of “Aaa”, “Aa”, “A” and “Baa” and S&P’s rating categories of “AAA”, “AA”, “A” and “BBB” (in each case, without modification by the applicable numeral or other modifier) refer to and include the respective rating categories correlative thereto if any or all of such rating agencies have changed or modified their generic rating categories or if they no longer rate the ARCs and have been replaced.

“ARCs” means each Subseries of the Senior Series 2003A Bonds while such Subseries is outstanding as Auction Rate Certificates.

“Auction” means each periodic implementation of the Auction Procedures on an Auction Date.

“Auction Agency Agreement” means the Auction Agency Agreement dated as of May 1, 2003 among the Corporation, the Trustee and the Auction Agent and any similar agreement with a successor Auction Agent, in each case as from time to time amended or supplemented.

“Auction Agent” means any person appointed as such pursuant to the Series 2003A Bond Resolution.

“Auction Date” means for the Senior Series 2003A-1 Bonds outstanding as ARCs, July 3, 2003; for the Senior Series 2003A-2 Bonds outstanding as ARCs, July 10, 2003; and thereafter, for each successive 35-day Auction Period, the Business Day immediately preceding the first day of each respective Interest Period other than:

- (a) each Interest Period commencing after the ownership of the ARCs is no longer maintained in book-entry form by the Depository;
- (b) each Interest Period commencing after the occurrence and during the continuance of a Payment Default; or
- (c) each Interest Period commencing less than the Applicable Number of Business Days after the cure or waiver of a Payment Default

Notwithstanding the foregoing, the Auction Date for one or more Auction Periods may be changed pursuant to the Series 2003A Bond Resolution.

“Auction Period” means, with respect to any ARCs, an Interest Period (after the Initial Interest Period) of generally thirty-five (35) days that commences on a Friday (or the day following the last day of the prior Auction Period, if the prior Auction Period does not end on a Thursday) and ending on (and including) a Thursday (unless such Thursday is not followed by a Business Day, in which case such Auction Period will end on the next succeeding day that is followed by a Business Day, as adjusted, pursuant to the Series 2003A Bond Resolution.

“Auction Procedures” means means the procedures set forth in Exhibit A to the Series 2003A Bond Resolution, as summarized in this Official Statement under “AUCTION RATE CERTIFICATES” and in this Appendix F.

“Auction Rate” means the rate of interest per annum on any Auction Date that results from the implementation of the Auction Procedures.

“Authorized Denominations” means with respect to the ARCs, \$50,000 or any integral multiple thereof.

“Available ARCs” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

“Bid” shall have the meaning set forth in this Appendix F under the heading “*Order By Existing Owners and Potential Owners.*”

“Bidder” shall have the meaning set forth in this Appendix F under the heading “*Order By Existing Owners and Potential Owners.*”

“Broker-Dealer” means with respect to the Senior Series 2003A Bonds outstanding as ARCs, UBS PaineWebber Inc., or any other broker or dealer (each as defined in the Securities Exchange Act of 1934, as amended), commercial bank or other entity permitted by law to perform the functions required of a Broker-Dealer set forth in the Auction Procedures that (a) is a Participant (i.e., a member of, or participant in, DTC or any successor securities depository) or an affiliate of a Participant, (b) has a minimum capital stock, surplus and undivided profits of \$50,000,000, (c) has been selected by the Corporation with the approval of the Market Agent (which approval shall not be unreasonably withheld), and (d) has entered into a Broker-Dealer Agreement with the Auction Agent that remains effective.

“Broker-Dealer Agreement” means the Broker-Dealer Agreement dated as of May 1, 2003 between the Auction Agent and the Broker-Dealer and each other agreement between the Auction Agent and a Broker-Dealer, approved by the Corporation, pursuant to which the Broker-Dealer agrees to participate in Auctions as set forth in the Auction Procedures, as from time to time amended or supplemented.

“Business Day” means any day other than: (i) with respect to ARCs, April 14, April 15, December 30, December 31, and such other dates as may be agreed to in writing by the Market Agent, the Auction Agent, the Broker-Dealer and the Corporation; and (ii) for all other purposes, a Saturday, Sunday, holiday or day on which banks in the City of New York, New York, or the New York Stock Exchange, the Trustee or the Auction Agent, are authorized or permitted by law or executive order to close.

“Change of Preference Law” means, with respect to any Owner of ARCs, any amendment to the Code or other statute enacted by the Congress of the United States or any temporary, proposed or final regulation promulgated by the United States Treasury after the original issuance date of the Senior Series 2003A Bonds that (a) changes or would change any deduction, credit or other allowance allowable in computing liability for any federal tax with respect to, or (b) imposes or would impose or reduces or would reduce or increases or would increase any federal tax (including, but not limited to, preference or excise taxes) upon, any interest earned by any Owner of

ARCs, the interest on which was excluded from gross income for federal income tax purposes under Section 103 of the Code.

“Default Rate”, on any date of determination, means the interest rate per annum equal to the lesser of (a) the Applicable Percentage of the Kenny Index and (b) the Maximum Interest Rate.

“Existing Owner” means (a) with respect to and for the purpose of dealing with the Auction Agent in connection with an Auction, a Person who is a Broker-Dealer listed in the Existing Owner Registry at the close of business on the Business Day immediately preceding the Auction Date for such Auction, and (b) with respect to and for the purpose of dealing with the Broker-Dealer in connection with an Auction, a Person who is a Beneficial Owner of ARCs.

“Existing Owner Registry” means the registry of Persons who are Existing Owners maintained by the Auction Agent as provided in the Auction Agency Agreement.

“Favorable Opinion” means a Counsel’s Opinion addressed to the Corporation and the Trustee to the effect that the action proposed to be taken is authorized or permitted by the Series 2003A Bond Resolution and will not adversely affect any exclusion from gross income for federal income tax purposes of interest on the Senior Series 2003A Bonds.

“Fixed Rate” means with respect to a Series of Bonds, the fixed rate of interest borne by such series of Bonds on and after the Fixed Rate Conversion Date and determined in accordance with applicable provisions the Series 2003A Bond Resolution.

“Fixed Rate Conversion” means the conversion of any series of the ARCs to Bonds bearing interest at a Fixed Rate as provided in the Series 2003A Bond Resolution.

“Fixed Rate Conversion Date” means the date on which a Fixed Rate Conversion becomes effective.

“Hold Order” shall have the meaning set forth in this Appendix F under the heading “*Order By Existing Owners and Potential Owners.*”

“Initial Interest Period” means, with respect to the Senior Series 2003A-1 Bonds, the period from and including the Issue Date and ending on and including July 6, 2003, and with respect to the Senior Series 2003A-2 Bonds, the period from and including the Issue Date and ending on and including July 10, 2003.

“Interest Payment Date” means with respect to the Senior Series 2003A Bonds, while Outstanding as ARCs, each May 1 and November 1, commencing November 1, 2003, except as changed as described in the Series 2003A Bond Resolution, and also means the maturity date thereof, or if any such date is not a Business Day, the next succeeding Business Day (but only for interest accrued through the preceding April 30 or October 31, as the case may be); provided, however, that any redemption date prior to the Fixed Rate Conversion Date or the Variable Rate Conversion Date (if not otherwise an Interest Payment Date, and then only with respect to the Bonds being redeemed) shall also be an Interest Payment Date.

“Interest Period” means, with respect to the ARCs, the Initial Period and thereafter, (a) unless otherwise changed pursuant to the Series 2003A Bond Resolution, the period commencing on a Friday (or the Business Day following the last day of the prior Interest Period, if the prior Interest Period does not end on a Thursday) and ending on (and including) a Thursday (unless such Thursday is not followed by a Business Day, in which case such Interest Period will end on the next succeeding day that is followed by a Business Day, and (b) if the Interest Period is changed as provided in the Series 2003A Bond Resolution, such period commencing on an Interest Payment Date and ending on but excluding the next succeeding Interest Payment Date.

“Kenny Index” means the index most recently made available by Kenny S&P Evaluation Services (“Kenny”) or any successor thereto (the “Indexing Agent”) based upon 30-day yield evaluations at par of securities,

the interest on which is excluded from gross income for federal income tax purposes under the Code, of not less than five “Intermediate Grade” component issuers selected by the Indexing Agent, which shall include, without limitation, issuers of general obligation bonds. The specific issuers included among the component issuers may be changed from time to time by the Indexing Agent in its discretion. The securities on which the Kenny Index is based shall not include any securities the interest on which is subject to a “minimum tax” or similar tax under the Code, unless all such securities are subject to such tax. In the event that Kenny no longer publishes an index satisfying the above definition of the Kenny Index or the Market Agent reasonably concludes that the Kenny Index will not be announced in a timely manner, then the Market Agent shall announce a rate based upon the same criteria used by Kenny to determine the Kenny Index and the rate announced by the Market Agent for each Auction Date thereafter shall be used in lieu of the Kenny Index for each Auction Date.

“Market Agent” means the market agent or market agents appointed pursuant to the Series 2003A Bond Resolution and its or their successors or assigns.

“Market Agent Agreement” means the Market Agent Agreement dated as of May 1, 2003 between the Corporation and the Market Agent and any similar agreement with a successor Market Agent, in each case as from time to time amended or supplemented.

“Maximum Interest Rate” means the lesser of: (i) 12% per annum (or such higher rate, not in excess of 18% as may be provided by amendment of the Series 2003A Bond Resolution upon the receipt by the Corporation of a Favorable Opinion); or (ii) the maximum rate of interest permitted by the laws of the Commonwealth.

“Maximum Rate”, on any date of determination with respect to ARCs, means the interest rate per annum equal to the lesser of:

- (a) the Applicable Percentage of the higher of (i) the After-Tax Equivalent Rate on such date and (ii) the Kenny Index on such date; and
- (b) the Maximum Interest Rate;

in each case rounded to the nearest one thousandth (.001) of 1%.

“Order” shall have the meaning set forth in this Appendix F under the heading “*Order By Existing Owners and Potential Owners.*”

“Payment Default” means failure by the Corporation to make payment of interest and premium, if any, on, and principal of, the ARCs when due.

“Potential Owner” means any Person, (including any Existing Owner that is (a) a Broker-Dealer when dealing with an Auction Agent and (b) a potential Beneficial Owner when dealing with a Broker-Dealer), who may be interested in acquiring ARCs (or, in the case of an Existing Owner thereof, an additional principal amount of ARCs).

“Record Date” means (a) so long as Interest Payment Dates are specified to occur at the end of each Auction Period, the Applicable Number of Business Days immediately preceding each Interest Payment Date and (b) if and for so long as interest is payable semiannually with respect to the ARCs, one Business Day prior to each Interest Payment Date.

“Redemption Date”, when used with respect to ARCs to be redeemed, means the date fixed for redemption.

“Remarketing Agent” means, with respect to the ARCs, UBS PaineWebber Inc., or such other remarketing agent appointed by the Corporation pursuant to the Series 2003A Bond Resolution.

“Remarketing Agreement” means the remarketing agreement among the Corporation and the Remarketing Agent in a form satisfactory to the Trustee, the Corporation and the Liquidity Facility Provider, if any.

“Sell Order” shall have the meaning set forth in this Appendix F under the heading “*Order By Existing Owners and Potential Owners.*”

“Statutory Corporate Tax Rate” means, as of any date of determination, the highest tax rate bracket (expressed in decimals) now or hereafter applicable in each taxable year on the taxable income of every corporation as set forth in Section 11 of the Code or any successor section without regard to any minimum additional tax provision or provisions regarding changes in rates during a taxable year, which on the date hereof is 35%.

“Submission Deadline” means 1:00 p.m. (New York City time), on any Auction Date or such other time on any Auction Date by which Broker-Dealers are required to submit Orders to the Auction Agent, as specified by the Auction Agent from time to time.

“Submitted Bid” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

“Submitted Hold Order” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

“Submitted Order” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

“Submitted Sell Order” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

“Sufficient Clearing Bids” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

“Undelivered Bonds” means Bonds that are deemed to have been purchased as provided in the Series 2003A Bond Resolution, but which have not been surrendered to the Trustee.

“Variable Rate” means any interest rate borne by any Series 2003A Bonds that is not a Fixed Rate or an Auction Rate.

“Variable Rate Conversion ” means the conversion of the ARCs to Bonds bearing interest at a Variable Rate (other than an Auction Rate) as provided in the Series 2003A Bond Resolution.

“Variable Rate Conversion Date” means the date on which a Variable Rate Conversion becomes effective.

“Winning Bid Rate” shall have the meaning set forth in this Appendix F under the heading “*Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*”

## **Auction Procedures**

Prior to a Fixed Rate Conversion Date or a Variable Rate Conversion Date, Auctions shall be conducted on each Auction Date (other than the Auction Date immediately preceding (a) each Interest Period commencing after the ownership of the ARCs is no longer maintained in book-entry form by the Depository; (b) each Interest Period commencing after the occurrence and during the continuance of a Payment Default; or (c) any Interest Period commencing less than two Business Days after the cure of a Payment Default). If there is an Auction Agent on such Auction Date, Auctions shall be conducted in the following manner:

- (a) *Orders By Existing Owners and Potential Owners.*



(i) Prior to the Submission Deadline on each Auction Date:

(A) each Existing Owner of ARCs may submit to a Broker-Dealer by telephone or otherwise any information as to: (1) the principal amount of Outstanding ARCs, if any, held by such Existing Owner that such Existing Owner desires to continue to hold without regard to the Auction Rate for the next succeeding Interest Period; (2) the principal amount of Outstanding ARCs, if any, that such Existing Owner offers to sell if the Auction Rate for the next succeeding Interest Period shall be less than the rate per annum specified by such Existing Owner; and/or (3) the principal amount of Outstanding ARCs, if any, held by such Existing Owner that such Existing Owner offers to sell without regard to the Auction Rate for the next succeeding Interest Period, and

(B) one or more Broker-Dealers may contact Potential Owners to determine the principal amount of ARCs that each such Potential Owner offers to purchase if the Auction Rate for the next succeeding Interest Period shall not be less than the rate per annum specified by such Potential Owner.

For the purposes hereof, the communication to a Broker-Dealer of information referred to in clause (A)(1), (A)(2), (A)(3) or (B) of this subsection (a)(i) is hereinafter referred to as an "Order" and collectively as "Orders." Each Existing Owner and each Potential Owner placing an Order is hereinafter referred to as a "Bidder" and collectively as "Bidders"; an Order containing the information referred to in (x) clause (A)(1) of this subsection (a)(i) is hereinafter referred to as a "Hold Order" and collectively as "Hold Orders"; (y) clause (A)(2) or (B) of this subsection (a)(i) is hereinafter referred to as a "Bid" and collectively as "Bids"; and (z) clause (A)(3) of this subsection (a)(i) is hereinafter referred to as a "Sell Order" and collectively as "Sell Orders".

(ii) (A) Subject to the provisions of subsection (b) below, a Bid by an Existing Owner shall constitute an irrevocable offer to sell: (1) the principal amount of Outstanding ARCs specified in such Bid if the Auction Rate determined shall be less than the rate specified in such Bid; or (2) such principal amount or a lesser principal amount of Outstanding ARCs to be determined as set forth in clause (D) of paragraph (i) of subsection (d) below, if the Auction Rate determined shall be equal to the rate specified in such Bid; or (3) such principal amount or a lesser principal amount of Outstanding ARCs to be determined as set forth in clause (C) of paragraph (ii) of subsection (d) below if the rate specified shall be higher than the Maximum Rate and Sufficient Clearing Bids have not been made.

(B) Subject to the provisions of subsection (b) below, a Sell Order by an Existing Owner shall constitute an irrevocable offer to sell: (i) the principal amount of Outstanding ARCs specified in such Sell Order; or (2) such principal amount or a lesser principal amount of Outstanding ARCs to be determined as set forth in clause (C) of paragraph (ii) of subsection (d) below if Sufficient Clearing Bids have not been made.

(C) Subject to the provisions of subsection (b) below, a Bid by a Potential Owner shall constitute an irrevocable offer to purchase: (1) the principal amount of Outstanding ARCs specified in such Bid if the Auction Rate determined shall be higher than the rate specified in such Bid; or (2) such principal amount or a lesser principal amount of Outstanding ARCs to be determined as set forth in clause (E) of paragraph (i) of subsection (d) below if the Auction Rate determined shall be equal to the rate specified in such Bid.

(b) *Submission by Broker-Dealers to the Auction Agent.*

(i) Each Broker-Dealer shall submit in writing to the Auction Agent prior to the Submission Deadline on each Auction Date all Orders obtained by such Broker-Dealer and shall specify with respect to each such Order:

(A) the name of the Bidder placing such Order,

(B) the aggregate principal amount of ARCs that are the subject of such Order,

(C) to the extent that such Bidder is an Existing Owner: (1) the principal amount of ARCs, if any, subject to any Hold Order placed by such Existing Owner; (2) the principal amount of ARCs, if any, subject to any Bid placed by such Existing Owner and the rate specified in such Bid; and (3) the principal amount of ARCs, if any, subject to any Sell Order placed by such Existing Owner, and

(D) to the extent such Bidder is a Potential Owner, the rate and amount specified in such Potential Owner's Bid.

(ii) If any rate specified in any Bid contains more than three figures to the right of the decimal point, the Auction Agent shall round such rate up to the next higher one-thousandth (.001) of 1%.

(iii) If an Order or Orders covering all Outstanding ARCs held by any Existing Owner is not submitted to the Auction Agent prior to the Submission Deadline, the Auction Agent shall deem a Hold Order to have been submitted on behalf of such Existing Owner covering the principal amount of Outstanding ARCs held by such Existing Owner and not subject to an Order submitted to the Auction Agent.

(iv) None of the Corporation, the Trustee nor the Auction Agent shall be responsible for any failure of a Broker-Dealer to submit an Order to the Auction Agent on behalf of any Existing Owner or Potential Owner.

(v) If any Existing Owner submits through a Broker-Dealer to the Auction Agent one or more Orders covering in the aggregate more than the principal amount of Outstanding ARCs held by such Existing Owner, such Orders shall be considered valid as follows and in the following order of priority:

(A) all Hold Orders shall be considered valid, but only up to and including the aggregate principal amount of ARCs held by such Existing Owner, and if the aggregate principal amount of ARCs subject to such Hold Orders exceeds the aggregate principal amount of ARCs held by such Existing Owner, the aggregate principal amount of ARCs subject to each such Hold Order shall be reduced pro rata to cover the aggregate principal amount of Outstanding ARCs held by such Existing Owner;

(B) (1) any Bid shall be considered valid up to and including an amount equal to the excess of the principal amount of Outstanding ARCs held by such Existing Owner over the aggregate principal amount of ARCs subject to any Hold Orders referred to in clause (A) of this paragraph (v); (2) subject to subclause (1) of this clause (B), if more than one Bid with the same rate is submitted on behalf of such Existing Owner and the aggregate principal amount of Outstanding ARCs subject to such Bids is greater than such excess; such Bids shall be considered valid up to and including an amount equal to the amount of such excess and the stated amount of ARCs subject to each Bid with the same rate shall be reduced pro rata to cover the stated amount of ARCs equal to such excess; (3) subject to subclauses (1) and (2) of this clause (B), if more than one Bid with

different rates is submitted on behalf of such Existing Owner, such Bids shall be considered valid first in the ascending order of their respective rates until the highest rate is reached at which such excess exists and then at such rate up to and including an amount equal to the amount of such excess; and (4) in any such event, the aggregate principal amount of Outstanding ARCs, if any, subject to Bids not valid under this clause (B) shall be treated as the subject of a Bid by a Potential Owner at the rate therein specified; and

(C) all Sell Orders shall be considered valid up to and including an amount equal to the excess of the principal amount of Outstanding ARCs held by such Existing Owner over the aggregate principal amount of ARCs subject to valid Hold Orders referred to in clause (A) of this paragraph (v) and valid Bids referred to in clause (B) of this paragraph (v).

(vi) If more than one Bid for ARCs is submitted on behalf of any Potential Owner, each Bid submitted shall be a separate Bid with the rate and principal amount therein specified.

(vii) Any Bid or Sell Order submitted by, or on behalf of, an Existing Owner covering an aggregate principal amount of ARCs not equal to an Authorized Denomination therefor shall be rejected and shall be deemed a Hold Order. Any Bid submitted by a Potential Owner covering an aggregate principal amount of ARCs not equal to an Authorized Denomination therefor shall be rejected.

(viii) Any Bid submitted by an Existing Owner or a Potential Owner specifying a rate lower than the All Hold Rate shall be treated as a Bid specifying the All Hold Rate and any such Bid shall be considered as valid and shall be selected in the ascending order of the respective rates in the Submitted Bids.

(ix) An Existing Owner that offers to purchase additional ARCs is, for purposes of such offer, treated as a Potential Owner.

(x) Any Bid or Sell Order submitted by an Existing Owner covering an aggregate principal amount of ARCs not equal to an Authorized Denomination shall be rejected and shall be deemed a Hold Order. Any Bid submitted by a Potential Owner covering an aggregate principal amount of ARCs not equal to an Authorized Denomination shall be rejected.

(xi) Any Bid submitted by an Existing Holder or a Potential Holder specifying a rate higher than the Maximum Interest Rate will (A) be treated as a Sell Order if submitted by an Existing Owner and (B) not be accepted if submitted by a Potential Owner.

(xii) Any Order submitted in an Auction by a Broker-Dealer to the Auction Agent before the Submission Deadline on any Auction Date shall be irrevocable.

(c) *Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.*

(i) Not earlier than the Submission Deadline on each Auction Date, the Auction Agent shall assemble all valid Orders submitted or deemed submitted to it by the Broker-Dealers (each such Order as submitted or deemed submitted by a Broker-Dealer being hereinafter referred to individually as a "Submitted Hold Order," a "Submitted Bid" or a "Submitted Sell Order," as the case may be, or as a "Submitted Order" and collectively as "Submitted Hold Orders," "Submitted Bids" or "Submitted Sell Orders," as the case may be, or as "Submitted Orders") and shall determine:

(A) the excess of the total principal amount of Outstanding ARCs over the sum of the aggregate principal amount of Outstanding ARCs subject to Submitted Hold Orders (such excess being hereinafter referred to as the "Available ARCs"); and

(B) from such Submitted Orders whether (1) the aggregate principal amount of Outstanding ARCs subject to Submitted Bids by Potential Owners specifying one or more rates equal to or lower than the Maximum Rate; exceeds or is equal to the sum of: (2) the aggregate principal amount of Outstanding ARCs subject to Submitted Bids by Existing Owners specifying one or more rates higher than the Maximum Rate; and (3) the aggregate principal amount of Outstanding ARCs subject to Submitted Sell Orders;

(in the event such excess or such equality exists, other than because the sum of the principal amounts of ARCs in subclauses (2) and (3) above is zero because all of the Outstanding ARCs are subject to Submitted Hold Orders, such Submitted Bids described in subclause (1) above being hereinafter referred to collectively as “Sufficient Clearing Bids”); and

(C) if Sufficient Clearing Bids have been made, the lowest rate specified in such Submitted Bids (which shall be the “Winning Bid Rate”) such that if: (1)(aa) each such Submitted Bid from Existing Owners specifying such lowest rate and (bb) all other Submitted Bids from Existing Owners specifying lower rates were rejected, thus entitling such Existing Owners to continue to hold the principal amount of ARCs subject to such Submitted Bids; and (2)(aa) each such Submitted Bid from Potential Owners specifying such lowest rate and (bb) all other Submitted Bids from Potential Owners specifying lower rates were accepted; the result would be that such Existing Owners described in subclause (I) above would continue to hold an aggregate principal amount of Outstanding ARCs that, when added to the aggregate principal amount of Outstanding ARCs to be purchased by such Potential Owners described in subclause (2) above, would equal not less than the Available ARCs.

(ii) Promptly after the Auction Agent has made the determinations pursuant to paragraph (i) of this subsection (c), the Auction Agent shall advise the Trustee and the Broker-Dealer of the Maximum Rate and the All Hold Rate and the components thereof on the Auction Date and, based on such determinations, the Auction Rate for the next succeeding Interest Period (the “Auction Rate”) as follows:

(A) if Sufficient Clearing Bids have been made, that the Auction Rate for the next succeeding Interest Period shall be equal to the Winning Bid Rate so determined;

(B) if Sufficient Clearing Bids have not been made (other than because all of the Outstanding ARCs are subject to Submitted Hold Orders), that the Auction Rate for the next succeeding Interest Period shall be equal to the Maximum Rate; or

(C) if all Outstanding ARCs are subject to Submitted Hold Orders, that the Auction Rate for the next succeeding Interest Period shall be equal to the All Hold Rate.

(d) *Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of ARCs.* Existing Owners shall continue to hold the principal amount of ARCs that are subject to Submitted Hold Orders, and, based on the determinations made pursuant to paragraph (i) of subsection (c), Submitted Bids and Submitted Sell Orders shall be accepted or rejected and the Auction Agent shall take such other action as set forth below:

(i) If Sufficient Clearing Bids have been made, all Submitted Sell Orders shall be accepted and, subject to the provisions of paragraph (iv) of this subsection (d), Submitted Bids shall be accepted or rejected as follows in the following order of priority and all other Submitted Bids shall be rejected:

(A) Existing Owners' Submitted Bids specifying any rate that is higher than the Winning Bid Rate shall be accepted, thus requiring each such Existing Owner to sell the aggregate principal amount of ARCs subject to such Submitted Bids;

(B) Existing Owners' Submitted Bids specifying any rate that is lower than the Winning Bid Rate shall be rejected, thus entitling each such Existing Owner to continue to hold the aggregate principal amount of ARCs subject to such Submitted Bids;

(C) Potential Owners' Submitted Bids specifying any rate that is lower than the Winning Bid Rate shall be accepted, thus requiring such Potential Owner to purchase the aggregate principal amount of ARCs subject to such Submitted Bids;

(D) each Existing Owner's Submitted Bid specifying a rate that is equal to the Winning Bid Rate shall be rejected, thus entitling such Existing Owner to continue to hold the aggregate principal amount of ARCs subject to such Submitted Bid, unless the aggregate principal amount of Outstanding ARCs subject to all such Submitted Bids shall be greater than the principal amount of ARCs (the "remaining principal amount") equal to the excess of the Available ARCs over the aggregate principal amount of ARCs subject to Submitted Bids described in clauses (B) and (C) of this paragraph (i), in which event such Submitted Bid of such Existing Owner shall be rejected in part, and such Existing Owner shall be entitled to continue to hold the principal amount of ARCs subject to such Submitted Bid, but only in an amount equal to the aggregate principal amount of ARCs obtained by multiplying the remaining principal amount by a fraction the numerator of which shall be the principal amount of Outstanding ARCs held by such Existing Owner subject to such Submitted Bid and the denominator of which shall be the sum of the principal amount of Outstanding ARCs subject to such Submitted Bids made by all such Existing Owners that specified a rate equal to the Winning Bid Rate; and

(E) each Potential Owner's Submitted Bid specifying a rate that is equal to the Winning Bid Rate shall be accepted but only in an amount equal to the principal amount of ARCs obtained by multiplying the excess of the aggregate principal amount of Available ARCs over the aggregate principal amount of ARCs subject to Submitted Bids described in clauses (B), (C) and (D) of this paragraph (i) by a fraction the numerator of which shall be the aggregate principal amount of Outstanding ARCs subject to such Submitted Bid and the denominator of which shall be the sum of the principal amounts of Outstanding ARCs subject to Submitted Bids made by all such Potential Owners that specified a rate equal to the Winning Bid Rate.

(ii) If Sufficient Clearing Bids have not been made (other than because all of the Outstanding ARCs are subject to Submitted Hold Orders), subject to the provisions of paragraph (iv) of this subsection (d), Submitted Orders shall be accepted or rejected as follows in the following order of priority and all other Submitted Bids shall be rejected:

(A) Existing Owners' Submitted Bids specifying any rate that is equal to or lower than the Maximum Rate shall be rejected, thus entitling such Existing Owners to continue to hold the aggregate principal amount of ARCs subject to such Submitted Bids;

(B) Potential Owners' Submitted Bids specifying any rate that is equal to or lower than the Maximum Rate shall be accepted, thus requiring each Potential Owner to purchase the aggregate principal amount of ARCs subject to such Submitted Bids; and

(C) each Existing Owner's Submitted Bid specifying any rate that is higher than the Maximum Rate and the Submitted Sell Order of each Existing Owner shall be accepted, thus entitling each Existing Owner that submitted any such Submitted Bid or Submitted Sell Order to sell the ARCs subject to such Submitted Bid or Submitted Sell Order, but in both cases only in an amount equal to the aggregate principal amount of

ARCs obtained by multiplying the aggregate principal amount of ARCs subject to Submitted Bids described in clause (B) of this paragraph (ii) by a fraction the numerator of which shall be the aggregate principal amount of Outstanding ARCs held by such Existing Owner subject to such Submitted Bid or Submitted Sell Order and the denominator of which shall be the aggregate principal amount of Outstanding ARCs subject to all such Submitted Bids and Submitted Sell Orders.

(iii) If all Outstanding ARCs are subject to Submitted Hold Orders, all Submitted Bids shall be rejected.

(iv) If, as a result of the procedures described in paragraph (i) or (ii) above, any Existing Owner would be entitled or required to sell, or any Potential Owner would be entitled or required to purchase, a principal amount of ARCs that is not equal to an Authorized Denomination therefor the Auction Agent shall, in such manner as, in its sole discretion, it shall determine, round up or down the principal amount of ARCs to be purchased or sold by any Existing Owner or Potential Owner so that the principal amount of ARCs purchased or sold by each Existing Owner or Potential Owner shall be equal to an Authorized Denomination, even if such allocation results in one or more of such Potential Owners not purchasing any ARCs.

(e) If, as a result of the procedures described in paragraph (i) or (ii) above, any Potential Owner would be entitled or required to purchase less than an Authorized Denomination of ARCs, the Auction Agent shall, in such manner as in its sole discretion it shall determine, allocate ARCs for purchase among Potential Owners so that only ARCs in Authorized Denominations are purchased by any Potential Owner, even if such allocation results in one or more of such Potential Owners not purchasing any ARCs.

(f) Based on the results of each Auction, the Auction Agent shall determine the aggregate principal amount of ARCs to be purchased and the aggregate principal amount of ARCs to be sold by Potential Owners and Existing Owners on whose behalf each Broker-Dealer submitted Bids or Sell Orders and, with respect to each Broker-Dealer, to the extent that such aggregate principal amount of ARCs to be sold differs from such aggregate principal amount of ARCs to be purchased, determine to which other Broker-Dealer or Broker-Dealers acting for one or more purchasers such Broker-Dealer or Broker-Dealers shall deliver, or from which other Broker-Dealers acting for one or more sellers such Broker-Dealer shall receive, as the case may be, ARCs.

#### **Trustee and Corporation Not Responsible for Auction Agent, Market Agent and Broker-Dealers**

Neither the Trustee nor the Corporation will be liable or responsible for the actions of or failure to act by the Auction Agent, the Market Agent or any Broker-Dealer under the Resolutions or under the Auction Agency Agreement, the Market Agent Agreement or any Broker-Dealer Agreement, except as otherwise provided in any such agreement. The Trustee and the Corporation may conclusively rely upon any information required to be furnished by the Auction Agent, the Market Agent or any Broker-Dealer without undertaking any independent review or investigation of the truth or accuracy of such information.

## **Appendix G**

### **Settlement Procedures for the Senior Series 2003A Bonds**

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## APPENDIX G

### SETTLEMENT PROCEDURES FOR THE SENIOR SERIES 2003A BONDS

*If not otherwise defined below, capitalized terms used below will have the meanings given such terms in the Resolutions (and described in Appendix C of this Official Statement) and in Appendix F of this Official Statement. The procedures described in this Appendix G apply only to the Senior Series 2003A Bonds which are referred to in Appendix F as ARCs and apply to each Subseries of ARCs separately.*

(a) Not later than 3:00 p.m. on each Auction Date, the Auction Agent is required to notify by telephone the Broker-Dealers that participated in the Auction held on such Auction Date and submitted an Order on behalf of any Existing Owner or Potential Owner of:

- (i) the Auction Rate fixed for the next Interest Period;
- (ii) whether there were Sufficient Clearing Bids in such Auction;
- (iii) if such Broker-Dealer (a "Seller's Broker-Dealer") submitted a Bid or a Sell Order on behalf of an Existing Owner, whether such Bid or Sell Order was accepted or rejected, in whole or in part, and the principal amount of ARCs, if any, to be sold by such Existing Owner;
- (iv) if such Broker-Dealer (a "Buyer's Broker-Dealer") submitted a Bid on behalf of a Potential Owner, whether such Bid was accepted or rejected, in whole or in part, and the principal amount of ARCs, if any, to be purchased by such Potential Owner;
- (v) if the aggregate principal amount of ARCs to be sold by all Existing Owners on whose behalf such Broker-Dealer submitted Bids or Sell Orders exceeds the aggregate principal amount of ARCs to be purchased by all Potential Owners on whose behalf such Broker-Dealer submitted a Bid, the name or names of one or more other Buyer's Broker-Dealers (and the Participant, if any, of each such other Buyer's Broker-Dealer) acting for one or more purchasers of such excess principal amount of ARCs and the principal amount of ARCs to be purchased from one or more Existing Owners on whose behalf such Broker-Dealer acted by one or more Potential Owners on whose behalf each of such other Buyer's Broker-Dealers acted;
- (vi) if the principal amount of ARCs to be purchased by all Potential Owners on whose behalf such Broker-Dealer submitted a Bid exceeds the amount of ARCs to be sold by all Existing Owners on whose behalf such Broker-Dealer submitted a Bid or a Sell Order, the name or names of one or more Seller's Broker-Dealers (and the name of the agent member, if any, of each such Seller's Broker-Dealer) acting for one or more sellers of such excess principal amount of ARCs and the principal amount of ARCs to be sold to one or more Potential Owners on whose behalf such Broker-Dealer acted by one or more Existing Owners on whose behalf each of such Seller's Broker-Dealers acted;
- (vii) unless previously provided, a list of all Applicable ARCs Rates and related Interest Periods (or portions thereof) since the last Interest Payment Date; and
- (viii) the Auction Date for the next succeeding Auction.

(b) On each Auction Date, each Broker-Dealer that submitted an Order on behalf of any Existing Owner or Potential Owner shall:

- (i) advise each Existing Owner and Potential Owner on whose behalf such Broker-Dealer submitted a Bid or Sell Order in the Auction on such Auction Date whether such Bid or Sell Order was accepted or rejected, in whole or in part;

(ii) instruct each Potential Owner on whose behalf such Broker-Dealer submitted a Bid that was accepted, in whole or in part, to instruct such Bidder's Participant to pay to such Broker-Dealer (or its Participant) through the Securities Depository the amount necessary to purchase the principal amount of ARCs to be purchased pursuant to such Bid against receipt of such principal amount of ARCs;

(iii) in the case of a Broker-Dealer that is a Seller's Broker-Dealer, instruct each Existing Owner on whose behalf such Broker-Dealer submitted a Sell Order that was accepted, in whole or in part, or a Bid that was accepted, in whole or in part, to instruct such Existing Owner's Participant to deliver to such Broker-Dealer (or its Participant) through the Securities Depository the principal amount of ARCs to be sold pursuant to such Bid or Sell Order against payment therefor;

(iv) advise each Existing Owner on whose behalf such Broker-Dealer submitted an Order and each Potential Owner on whose behalf such Broker-Dealer submitted a Bid of the Auction Date for the next Interest Period;

(v) advise each Existing Owner on whose behalf such Broker-Dealer submitted an Order of the next Auction Date; and

(vi) advise each Potential Owner on whose behalf such Broker-Dealer submitted a bid that was accepted, in whole or in part, of the next Auction Date.

(c) On the basis of the information provided to it pursuant to paragraph (a) above, each Broker-Dealer that submitted a Bid or Sell Order in an Auction is required to allocate any funds received by it pursuant to paragraph (b)(ii) above, and any ARCs received by it pursuant to paragraph (b)(iii) above, among the Potential Owners, if any, on whose behalf such Broker-Dealer submitted Bids, the Existing Owners, if any, on whose behalf such Broker-Dealer submitted Bids or Sell Orders in such Auction, and any Broker-Dealers identified to it by the Auction Agent following such pursuant to paragraph (a)(v) or (a)(vi) above.

(d) On each Auction Date:

(i) each Potential Owner and Existing Owner with an Order in the Auction on such Auction Date shall instruct its Participant as provided in (b)(ii) or (b)(iii) above, as the case may be;

(ii) each Seller's Broker-Dealer that is not a Participant in the Securities Depository shall instruct its Participant to (A) pay through the Securities Depository to the Participant of the Existing Owner delivering ARCs to such Broker-Dealer following such Auction pursuant to (b)(iii) above the amount necessary, including accrued interest, if any, to purchase such ARCs against receipt of such ARCs, and (B) deliver such ARCs through the Securities Depository to a Buyer's Broker-Dealer (or its Participant) identified to such Seller's Broker-Dealer pursuant to (a)(v) above against payment therefor; and

(iii) each Buyer's Broker-Dealer that is not a Participant in the Securities Depository shall instruct its Participant to (A) pay through the Securities Depository to a Seller's Broker-Dealer (or its Participant) identified following such Auction pursuant to (a)(vi) above the amount necessary, including accrued interest, if any, to purchase the ARCs to be purchased pursuant to (b)(ii) above against receipt of such ARCs, and (B) deliver such ARCs through the Securities Depository to the Participant of the purchaser thereof against payment therefor.

(e) On the first Business Day of the Interest Period next succeeding each Auction Date:

(i) each Participant for a Bidder in the Auction on such Auction Date referred to in (d)(i) above shall instruct the Securities Depository to execute the transactions described under (b)(ii) or (b)(iii) above for such Auction, and the Securities Depository shall execute such transactions;

(ii) each Seller's Broker-Dealer or its Participant shall instruct the Securities Depository to execute the transactions described in (d)(ii) above for such Auction, and the Securities Depository shall execute such transactions; and

(iii) each Buyer's Broker-Dealer or its Participant shall instruct the Securities Depository to execute the transactions described in (d)(iii) above for such Auction, and the Securities Depository shall execute such transactions.

(f) If an Existing Owner selling ARCs in an Auction fails to deliver such ARCs (by authorized book-entry), a Broker-Dealer may deliver to the Potential Owner on behalf of which it submitted a Bid that was accepted a principal amount of ARCs that is less than the principal amount of ARCs that otherwise was to be purchased by such Potential Owner (but only in Authorized Denominations). In such event, the principal amount of ARCs to be so delivered shall be determined solely by such Broker-Dealer (but only in Authorized Denominations). Delivery of such lesser principal amount of ARCs shall constitute good delivery. Notwithstanding the foregoing terms of this paragraph (I), any delivery or nondelivery of ARCs that shall represent any departure from the results of an Auction, as determined by the Auction Agent, shall be of no effect unless and until the Auction Agent shall have been notified of such delivery or nondelivery in accordance with the provisions of the Auction Agency Agreement and each Broker-Dealer Agreement.

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